OXFORD

Glimpses of INDIAN ECONOMIC POLICY

An Insider's View

I.G. PATEL

PATEL

Glimpses of INDIAN ECONOMIC POLICY

OXFORD

OTHER OXFORD BOOKS

S. GUHAN
edited by S. Subramanian
India's Development Experience

T.N. SRINIVASAN
edited by N.S.S. Narayana
Economic Policy and State Intervention

DEBRAJ RAY
Development Economics
(Oxford India Paperbacks)

TERENCE J. BYRES (editor)
The Indian Economy
Major Debates since Independence
(Oxford India Paperbacks)

K. BASU, P. PATTANAIK, AND K. SUZUMURA (editors)
Choice, Welfare, and Development
A Festschrift in Honour of Amartya Sen
(Oxford India Paperbacks)

ISHER JUDGE AHLUWALIA AND I.M.D. LITTLE (editors)
India's Economic Reforms and Development
Essays for Manmohan Singh
(Oxford India Paperbacks)

ISBN 019565885-X

9 780195 658859

OXFORD
UNIVERSITY PRESS

www.oup.com

Glimpses of Indian Economic Policy

To
My two sets of parents

Glimpses of Indian Economic Policy

An Insider's View

I.G. Patel

OXFORD
UNIVERSITY PRESS

OXFORD
UNIVERSITY PRESS
YMCA Library Building, Jai Singh Road, New Delhi 110001

Oxford University Press is a department of the University of Oxford. It furthers the University's objective of excellence in research, scholarship, and education by publishing worldwide in

Oxford New York

Athens Auckland Bangkok Bogota Buenos Aires Cape Town Chennai Dar es Salaam Delhi Florence Hong Kong Istanbul Karachi Kolkata Kuala Lumpur Madrid Melbourne Mexico City Mumbai Nairobi Paris São Paulo Shanghai Singapore Taipei Tokyo Toronto Warsaw

with an associated company in Berlin

Published in India
By Oxford University Press, New Delhi

First published by Oxford University Press 2002

ISBN 019 565885X

Typeset in A Garamond Regular 11.5 by 13.5
at Innovative Processors New Delhi 110 002
Printed at Roopak Printer, Delhi 110 032
Published by Manzar Khan, Oxford University Press
YMCA Library Building, Jai Singh Road, New Delhi 110 001

Preface

Having been associated, directly or indirectly, with the making of Indian economic policy for nearly five decades, I have often thought of writing an account of the evolution of economic policy in India since Independence.* It soon became clear, however, that this was a major enterprise, which required access to official documents and much assistance. Memory is always a treacherous guide, and I had followed scrupulously the civil service code and never carried any official papers home after relinquishing charge of the various posts I had occupied. It has not been possible so far to get access to official documents; and time and memory are slipping by.

I have, therefore, to write this monograph almost entirely from memory despite all the tricks it can play. There are things on which I can speak with some confidence even today; and I owe to my many mentors and colleagues the wonderful memories I have of my association with them. My own evolution as an economist, policy adviser and economic diplomat may not be without some general interest or significance. And there are some seminal events in recent Indian economic history like the Second Five Year Plan, the drift into foreign aid and a regime of controls, the response to the Chinese war and Gold Control, the 1966 devaluation, the nationalization of banks in 1969, the Bangladesh war of 1971, the

*Paris, 30 November 1999.

beginning of the cancer of systemic corruption, the politicization of economic life and institutions, and the response to the second oil crisis about which I can speak from experience not available to many. Hence this monograph: as much a tribute to others as a piece of my own biography, as much a historical account as a commentary on economic training, economic policy and indeed India and the world economy as a new millenium takes over from the last.

It is not as if I have not written earlier about many things commented upon here. The two volumes of my speeches and articles published by Macmillan and several scattered writings bear witness to my weakness for argument and articulation. But autumnal hues have shades different from those so striking in the spring or in summer; and truth—if there is such a thing—comes in many colours and shades. Besides, old men are even more garrulous; and that is where this preface and the justification for this monograph must rest.

The foregoing preface was written as an invitation to myself to get on with the job.* The first three chapters of what follows were written in New York in December 1999 and January 2000 and the rest in London in May 2000. They have subsequently undergone several editorial and other checks and changes. But in substance, this monograph remains a product of hectic recollection and reflection, and I have retained the references to the dates and places where the initial drafting was done to underscore the nature—and indeed, the limitations—of this enterprise. I would crave the indulgence of the reader for any lapses in recall that still remain.

The period covered is from my student days to my relinquishing charge as Governor of the Reserve Bank in 1982. Since then, I have been professionally associated with higher education, which is not within the scope of economic policy. I have also written at

*Baroda, 9 February 2001.

length on economic policy since 1982 as an 'outsider'; and much of it is already in the public domain. I have seen little reason, therefore, to revisit that territory here. For the same reason, the references to international institutions and my association with them have been limited to their relevance to Indian economic policy.

Manu Shroff and Alaknanda Patel have played their usual role of correcting and censoring everything I write. But this time they have been rather indulgent, in deference perhaps to the rather personal nature of this account, warts and all. My gratitude to them, therefore, is all the greater. The editors at OUP could not have been more helpful. I am grateful also to the referees for their valuable comments and suggestions, and I hope they are satisfied with my response. M.N. Sane has wrestled valiantly to transform my handwriting into neatly typed pages, and I am most indebted to him for his patience and care.

Contents

1

The Making of an Economist 1942–54

By the time I left for England in 1944 to study economics at Cambridge, I had already formed some rather inchoate, eclectic and indeed inconsistent views on India's economic problems and their solutions.* Many strands went into the making of these views: the controversies surrounding the nationalist movement, the cursory study of economics and, even more, of Indian economic problems required for my undergraduate degree from the University of Bombay, the impact of the Second World War and my particular family circumstances.

The Early Years

Those of us who grew up in the thirties and the early forties were torn between the economic views of Gandhiji and Nehru. Both had an appeal which was difficult to resist. Gandhiji's emphasis on rural areas, decentralized and small-scale production, village self-sufficiency, dignity of work, austerity, self-help, respect for all God's creation, including Nature, and above all, *Antyodaya*, that is, utmost attention to the well-being of the most deprived and downtrodden, had an obvious appeal to young minds. This was

*Washington, D.C., 2 December 1999.

not called socialism then. In fact, it was fashionable to talk of Gandhiji as an apologist for capitalism in view of his defence of private property and the consequent emphasis on trusteeship, which implied trust in the rich as well as regard for the rights and dignity of labour. Gandhiji, if you like, appealed to the heart, but not so much to the head.

Our heads then were full of dreams of a strong India—India strong industrially, if not militarily (we did not see the connection then), able to stand with its head held high among the nations of the world, India reversing the humiliation of the past two hundred years by making up for lost time. To most of us, this pointed to Nehru—and vaguely to socialism, but not to communism. Gandhiji's ideas on ends not justifying means could not be reconciled with the Hitler–Stalin pact; and it was not easy to take to our communist friends in India for whom overnight an imperial war became a people's war. That democracy stood between socialism and communism or that Gandhiji was, in fact, what many in the West would recognize as a Christian Socialist did not dawn on us then.

Subhash Chandra Bose created contradictory feelings in Gujarat. His rebellion against Gandhiji was not liked. Nor was there any love for the Germans and the Japanese, although we did not know in 1942 or 1943 much about the atrocities against the Jews. But we were all admiration for Subhash Babu's escape and joining hands with the Germans and the Japanese as a kind of insurance for India, just in case.

The Quit India movement of 1942 brought the Congress socialists into prominence. Jaya Prakash Narayan, Ashok Mehta, Achyut Patwardhan, Yusuf Meherally and Aruna Asaf Ali, to name just a few, impressed us by their bravery and disciplined defiance of the British. This admiration carried over into the vague belief that the Congress socialists pointed to a new path—better than and different from the worldview of Gandhiji, Nehru or the communists. But what exactly this path was, we knew not then—nor, sad to say, did the Congress socialists themselves then or later, which made them ineffective leaders and a forlorn hope. The ideas

invoked by the nationalist movement thus covered a wide canvas but did not point to a coherent and operational map for the future.

The Second World War and its impact on India also left deep scars on our minds. The war effort and the resulting export surplus led to a sharp rise in prices despite extensive controls. Economists like C.N. Vakil made a reputation by highlighting how monetary expansion, propelled then by the export surplus, leads to inflation which plays havoc with the lives of most people. What I once referred to as 'a very low margin of tolerance for inflation in India'[1] owes much to this war-time inflation and its association with the British. The counterpart was the firm belief that the sterling balances built up by India were the result of great sacrifice and hardship of millions of ordinary Indians, and that this debt should be fully and fairly honoured by the British after the war. The sterling balances were also seen as an important source for post-war reconstruction and for initiating the process of development.

The war also saw the birth of very high rates of taxation and economic controls virtually unknown in India before. The regime of exchange controls created then needed little elaboration after the war. Not just external trade but internal trade and movement of essential commodities, particularly foodgrains, were also controlled. In major cities, several articles of daily consumption were rationed. It is not often appreciated what a long shadow all this cast on post-war economic policy.[2] High taxes and controls were difficult to dismantle; and many civil servants and politicians acquired a taste for these. The Gandhian antipathy to controls had not asserted itself. On the other hand, the large-scale evasion of taxes and of controls and the enormous 'black' profits made by some and privation felt by many led to a certain distrust of, and even distaste for, Indian private trade and industry. There was perhaps some temptation to justify evasion of taxes in so far as they were heavy and levied by the British to aid the war effort. But the same could not be said about profiteering at the expense of the ordinary consumer. Rationing, even in the major cities, was perfunctory and ineffectively administered as was perhaps inevitable. The general belief that private trade and industry tend to evade

and exploit got a big boost during the war, and this attitude persisted to some extent for many years after the war.

The best that can be said about what we learnt of economic theory, economic history or economic policy during our undergraduate days in India is that while it was essentially impressionistic rather than rigorous or analytical, the impressions ranged over a very wide spectrum. We even had a paper on history of economic thought for the B.A. (Hons.) course of Bombay University, and the full paper on Indian Economics gave us a wealth of information on the entire range of economic activity in the country. Thus, about agriculture we knew not only of subdivision and fragmentation of holdings, but also of waterlogging, desalination and loss of soil fertility through destruction of forests, at least in hilly regions. Concern for conservation and enhancement of natural resources—if not for environment as a whole—was thus not unknown. We knew too that famines are caused as much by lack of income as by failure of monsoons, the two being, in fact, related. In industry, we were aware of the Managing Agency System, and in banking of the neglect of the needs of the rural areas and of small industry and of the 'drain' of savings from the rural to the urban areas. This was a kind of a parallel to the other 'drain' which obsessed us: from India to Britain. Concern for monopoly or concentration of economic power and the limitations of private banking were not thus purely post-war phenomena. There was, of course, in addition much reflection of the nationalist sentiment in the discussion of the independence of the Reserve Bank from the Government and in the exchange rate controversy about whether the rupee should be worth 1 sh. 6 d. (as it was) or 1 sh. 4 d. as the nationalists wanted. It is interesting to recall that the nationalists then (unlike some of the latter-day patriots) were not in favour of a macho view of the exchange rate but regarded a somewhat undervalued rate as an aid to industry and exports. Gyan Chand's *India's Teeming Millions*[3] had also done much to highlight the population problem.

I recall all this to underline that there is a certain continuity in our experience before independence and the post-war or post-

independence policies and that there is hardly anything which is altogether new in life. Only priorities and relative emphasis change with changing circumstances and experience. There is always another side to each proposition or policy, which may become more or less relevant at different times. What survives the vicissitudes of time and space perhaps are some aspects of human nature and, therefore, of human relationships. That may provide a key to understanding society as it develops. But the paths along which societies develop are varied and tortuous; and there is no simple or single road to social reform for all times and climes.

My individual family circumstances, which were by no means untypical, also left a deep impression. The regular arrival of siblings and its constricting impact as well as the forebodings of daunting responsibilities for the eldest son have forever made me a protagonist of smaller families. During the thirties, despite my father's very modest salary, we lived, if not in comfort, at least without any sense of deprivation. All that changed with the war and inflation and I have remained allergic to the argument that inflation is good for development, let alone equity. Perhaps not surprisingly, I have not felt equally concerned about the lot of many primary producers during the 'depressed' thirties as we did well by that phenomenon. Good fortune evokes no thought or protest or soul-searching, while hardship can be creative.

The British tended to explain India's economic backwardness largely in terms of its social customs and attitudes and religious beliefs and practices, in part at least to exonerate themselves from charges of neglect and worse. For that very reason, the nationalists were prone to overlook or underplay this aspect. My own experience made me question the nationalist view. All around one saw the economic consequences of dowry and inordinate expenses at the time of birth, marriage and death: the 'debt trap' that these created for so many families which were often driven to ruinous speculation or extortion by the so-called religious teachers, and the straitjacket in which the caste system kept vast sections of society. The havoc played by religious conflicts was yet to come; but the seeds were there for all to see.

We are yet to come to terms with our own weaknesses as a society: its culture, customs, beliefs and practices. Shutting an eye to them and focusing only on economic policies, is tantamount to overlooking the problems of implementation. Much is said these days, for example, about the neglect of primary education by the government. But are there also not social reasons why so many children are kept away from schools or removed so soon?

Traditionally, education has been valued in India. My own mother could just about read or write. But she made it clear that with no family land to divide or property to inherit, our own salvation lay in studying well and that as parents they would spare no effort or sacrifice if we were prepared to play our part. But there are large sections of our society even today which are not convinced that education, particularly of the girl child, is in the interest of the family and is worth some current sacrifice.

Education benefits the individual as well as the society. The responsibility, therefore, has to be owned by both. One has to go back to Gandhiji and somewhat away from Nehru, so to speak, to strike a right balance between the primary responsibilities of each of us, in whatever condition of life, for self-help and self-reform and that of the government to facilitate self-improvement without eroding the dignity of each individual and without encouraging a dependency syndrome. At the same time, those more fortunate have to be reminded of Gandhiji's views on trusteeship. Or, as Rabbi Hilel would put it: 'If I am not for myself, who is for me? If I am not for others, then what am I? If not now, when?'

*A Passage to Cambridge**

The idea of going to Cambridge for higher studies was first planted in my mind by Professor D. Ghosh who taught me elementary economics in Baroda during my Intermediate year at college. Professor Ghosh had had a distinguished career at Cambridge and had a well-deserved reputation as one of the few Indian economists who retained an interest in the latest developments in economic theory. He remained in Baroda for a little over a year and economics

*Washington, D.C., 7 December 1999.

was only a minor subject in the Intermediate Arts examination. But even the little exposure to his teaching was enough to arouse in me a real attraction to the subject. Before leaving Baroda, he took me to see the Dewan of Baroda, Shri V.T. Krishnamachari, and pleaded that I should be given a state scholarship to go to Cambridge when the time came. As far as economics is concerned, I have to acknowledge with pride and gratitude that Professor Ghosh was my first inspiration, *Adiguru*, and life-long well-wisher.

By the time I graduated in 1944, Cambridge seemed far away. The war was on; and I set my heart on going to the Bombay School of Economics for post-graduate studies. I did, however, send a hand-written letter to King's College, Cambridge, seeking admission and telling them briefly about myself. 'King's—and for that matter, Cambridge—were mere sounds to me then that I had heard from Professor Ghosh, and were vaguely associated in my mind with Keynes and with Joan Robinson. I did not even know that women could not be members of King's!

Getting financial assistance to study at Bombay proved a rather daunting and even humiliating affair which was suddenly resolved by my youthful brashness. R.D. Chokshi of Sir Dorab Tata Trust politely told me that they helped only science students and not arts graduates. I immediately proceeded to tell him that economics indeed was a science. He was so amused that he asked me to write an essay on the subject and promised to show it to his trustees. Lo and behold, they liked my essay and I landed a scholarship—my first real gain from a little knowledge of economics and my first acquaintance with the nature of Tata philanthropy!

I joined the Bombay School of Economics but soon thereafter, I got a letter from King's to say that I was admitted and that I could go there whenever it was possible. I knew that civilian traffic between India and England had stopped as a result of the war. But I went to Thomas Cook to enquire —and was greeted with some derisive laughter and reminded that there was a war going on. But they took down my name and address; and a few weeks later, I was informed that I could go if I could leave within a week. A ship had been converted to civilian use to evacuate the families of British missionaries in China; it was about to touch Calcutta and Bombay and had a few berths vacant.

It is difficult to convey what went on during the week of my departure—the excitement, the anxiety, the sheer magnitude of the arrangements and the adjustments to be made and the outpouring of support from so many quarters. My teacher, Professor V.S. Tilak, ensured that I got the Baroda State Scholarship; and Principal Romans of Baroda College approached the British Resident to procure the passport.[4] A friend in Bombay introduced me to knives and forks and scrambled eggs. My sisters packed what they thought I would need in a big trunk. But the biggest problem was to persuade my parents to let me go. How were they to let me—their eldest son—go when German submarines were busy plying the Mediterranean and the Atlantic, and German bombs were falling on London every night and there was no end to the war in sight? Professor Tilak tried to help by procuring an astrological forecast about my safety. But in the end, my parents found their own answer. They told me: 'We know what this means to you. If we let you go and something happens to you, the world will blame us. If we do not let you go and your chances in life are impaired, you will blame us. We will be able to take the blame of the world, but not your blame. You have our blessings. Please do whatever is needed for your studies and good health. We trust you. Do not worry about us.'

The long voyage of 48 days from September to November 1944, which took me from Bombay to UK, gave me time to ruminate about the past and to dream and prepare for the future. I knew from personal experience by then that it is not poverty but insecurity that demeans and degrades. As long as the needs are defined by custom and circumstance and are shared by those around you, it is possible to lead a civilized and dignified life based on values other than economic gain. But insecurity, whether due to sickness or large families or inflation, can corrode. In a different way, ambition too is unsettling. And when there is change all around you, ambition and a degree of dislocation or estrangement are to some extent inevitable. The process of urbanization had brought this home to many rural families as the literature of the time amply documents. Faced with insecurity, change and

ambition, people seek some comfort and solace in a sense of belonging, in having some firm roots—whether in the family or the caste or the community. Smaller loyalties—more visible and more within grasp—become necessary and serve as anchors in times of change and turbulence. But they are debilitating too. And how does one nurture a sense of nationhood in the midst of such myriad of loyalties? These thoughts which were in our minds in 1944 are perhaps not irrelevant even now. Globalization is only an extension of urbanization.

The two-year B.A. Honours course in Baroda had taught us little economics. In fact, there was not much teaching, thanks to the Quit India movement and the paucity of qualified teachers. But one good thing about having to learn on your own is that it forces you to read only a few things, to read them slowly and well and to try and make them pass through your own thought processes. On the voyage, I had with me a few books, which I had won as prizes for my B.A. results and which I had not read but now pored over slowly but avidly. For the first time, economics began to make sense.

The Social Framework by Hicks made me realize for the first time that 'an economy' was not just a random or disconnected set of activities but a 'system' where the different parts were interrelated in a certain way. Economics was about discovering the connections, which transformed the diverse activities into a system. Indeed, without some systematic connections, there could be no economy, no economics and no economic policy. There are, of course, various ways of defining the underlying system. One obvious way was to think of an economy as a system of interconnected markets—markets for final goods, intermediate goods and factors of production; markets—local or national or international; markets of exchange at a point of time or as between different points of time; markets for goods or for financial instruments. We were not aware then that the development of markets required appropriate legal and other institutions, social conventions and ingenuity in

developing different types of financial contracts and products, that a market economy is not a static stereotype but a dynamic, living, pulsating and changing act of creation to achieve certain individual and social ends. One cannot do without markets any more than one can do without breathing. But the air we breathe can be cleaner or more polluted.

Joan Robinson's *Theory of Imperfect Competition* provided an elegant and exciting exposition of one measure of 'cleanliness' or 'pollution' of markets, the cleanest being perfectly competitive markets and the pollutants, different kinds of imperfections. The task of good policy must be to remove the imperfections and make markets more and more competitive—or try and create conditions which provide an approximation to perfectly competitive markets. Abba Lerner's *Economics of Control* and James Meade's *Economic Analysis and Policy* made fascinating reading. Economics was something orderly; it also provided ways of making real economic life not just more orderly but more efficient and even more equitable, at least within the limits set by the initial distribution of income. Public policy in the shape of taxes, subsidies and controls had a rationale and could be given a concrete operational shape. I have not read these books again more recently. But the deep impression they made on me has persisted over many years of practical experience.

Keynes's *General Theory* opened another path for visualizing an economy as 'a system'—a system of aggregate demand and supply interacting with each other to make for changes in employment, incomes and prices. Truth to tell, my several readings of the General Theory on the ship did not lead to any clear grasp of what it was all about. I had to wait till I reached Cambridge and read some of the younger followers of Keynes to get excited about 'macroeconomics' in the way I had been about 'microeconomics'; the two terms themselves became better defined only later.

After all the excitement and adventure of the long voyage, the actual arrival in Cambridge early in November 1944—a few days

before my twentieth birthday—was an anticlimax and even painful. On landing at Greenock in Scotland, we had to surrender all our luggage to the customs—and I never saw it again.[5] I left for Cambridge by train with nothing but what was on me. I had to spend several hours at Bletchley at night where I had to change trains. Not even a cup of tea was available to warm the bitterly cold night. The women volunteers serving tea to soldiers in passing trains refused to serve me as I did not belong to the armed forces! Ultimately, I joined a group of farm workers seated around a fire at one end of the station. They asked me what we grow in India; and when I told them that we grow wheat, rice and all the rest, they said they would like to migrate to India. I had to inform them of the wages that they could expect, and one of them asked: 'What kind of a country is that? Who rules over you?' So much for the imperial race and the White Man's Burden!

At Cambridge, the first few days were torture with no heating at night. But soon, the senior tutor, Donald Beves sprang into action; and I had some clothes, some money till my scholarship arrived and a place to stay. I also began my tutorials with Gerald Shove and A.C. Pigou. The Cambridge tutorial system is justly famous. It teaches you not X or Y but how to think, and think logically. Shove was a master of this technique. He never told you what to read. Nor did he tell you what your answers lacked. He just marked the sentences where you had slipped in logic and read them out to you in context till you yourself noticed what was wrong. What was important was not how much you knew or read, but how much you assimilated as a part of your own thinking. Both of them were generous with their time; and Shove, in particular, made a deep impression on me by his humane and self-effacing personality. Keynes had predicted that Shove would be the Prime Minister of UK. Instead, he spent his life nursing his invalid wife and inspiring generations of students.

*Macro and Micro Economics**

In a sense, the study of economics at Cambridge for my B.A. (Honours) degree (1944–6) took me one step forward and half-a-

*Washington, D.C., 9 December 1999.

step backward. There was a shortage of teachers during the war which was partly compensated for in my first year (1944–5) by the presence of the London School of Economies (LSE) in Cambridge. The lectures were common and could be attended by students of both Cambridge and LSE. But the teachers were free to lecture on anything they liked—and barring some elementary lectures on 'Indifference Curve Analysis' by Professor Hayek, we were treated only to various aspects and versions and assessments of macroeconomics. Somehow, microeconomics faded away from our vision. This was hardly surprising from the practical point of view. In a war-time economy of controls and rationing, there was little need for a theory of allocation of resources.[6] The only practical problem was how to set the overall rations or ration-points and the relative prices in terms of money as well as points where some consumer choice was left; and this was a matter of adjustment by trial and error. I remember a question in my preliminary examination: How do you distribute your consumption between different items when they have money prices as well as prices in terms of points? The answer was simple: in an economy of shortages and forced savings, money prices and money incomes were irrelevant; it was the scarcer 'points-income' and 'point-prices' which set the stage.[7]

We did imbibe some more of microeconomics though by reading—particularly, Pigou's *Economics of Welfare*. Externalities and their links with public well-being and the interventions they pointed to were in line with what we had read of Lerner and Meade. The notion of public goods and non-appropriability of some costs and benefits and the policy conclusions that follow had an appeal; another question at the preliminary examination in 1945 was precisely on that. We were not, however, exposed to any systematic understanding of microeconomics even through good textbooks. For that, we had to await the post-war crop of American textbooks, above all, Samuelson and Stigler. Frankly, I read them well only when I had to teach economic theory at Baroda in 1949–50.

Even macroeconomics we pored over only as theory or a set of theorems. About its practical application during the war, Keynes's 'How to pay for the War' was enough. Macroeconomics as a tool for fine-tuning the economy required elaboration of a set of national accounts. Although Richard Stone had begun this work in Cambridge, I was to become aware of how to handle all that only after I went to work for the International Monetary Fund (IMF) in 1950. Till then, I had seen no actual budget or the balance sheet of a Central Bank, let alone balance of payments or a set of national accounts.

The macroeconomics we learnt was also largely of a closed economy—understandable enough during the war. In the spring of 1945, Kaldor gave five lectures on the extension of the general theory to an open economy. I remember being fascinated by them. But it was still non-operational stuff. It was only during my Ph.D. work that I read of the first attempts by Walter S. Salant and others to initiate the kind of work which later led to more precise and operational formulations through the 'absorption theory' first developed, to my knowledge, by Sidney Alexander, a young Harvard economist who taught me statistics in 1948 and who worked for the Fund for a short while in the early 1950s. Marcus Fleming was another innovator in the Fund in that line of analysis.

Looking back, my economics training at Cambridge was singularly devoid of operational or research skills. Let alone research methodology, we had only cursory exposure to correlation techniques and none to economic modelling through a set of differential equations—although I had statistics as a special paper for my B.A. examination in 1946. At Harvard,[8] they taught more advanced statistics; but my interests had by then shifted to the logical foundations of statistics (as of everything, thanks to Wittgenstein and Ayre). I have, I am afraid, remained virtually ignorant of, and averse to, the techniques of quantitative research. And I have been able to get by only because the scarcity of trained economists, created by the war, propelled some of us to very high positions rather early in life where we could leave that kind of laborious work to others! Sad to recall, but true.

What Cambridge did teach was how to read and think on your own and what the company of bright young minds can do. I owe much to Shove and Pigou for making me think, and to the

many friends I made for stimulating interactions with them. In my first year (1944–5), my only friends were at the LSE: the most prominent of these was K. N. Raj who did much by his wit and affection to relieve the tensions of a new life, and became a life-long friend. Rudolph Goldsmith introduced me to Western music. The end of the war in 1945 brought an influx of many bright and mature students to Cambridge and some of us soon became friends who met often and tossed the ball around. The group included Harry Johnson, Eric Russell, Robin Marris and Frank Davidson. All of us did well at Cambridge, and our friendship survived the many twists and turns our lives took in later years.

No account of my Cambridge years could be complete without a brief reference to a few other persons who left a great impression on me. Professor D.H. Robertson's lectures—all written in advance and read out—taught us that good economics and good style can go together. His advice that I should practise thinking and writing and teaching economics in Gujarati is something I should have followed, but did not. Even outside the classroom, he was most helpful and encouraging. Professor E.A.G. Robinson was my thesis supervisor whom I used sparingly; but his affection for me and for my daughter has been one of my life's treasures. P. Sraffa ran an after-dinner discussion group where he regaled us with his characteristic sarcasm: 'If interest is reward for waiting, thieves who wait till it is dark should be rewarded.'

On a different plane, the friendship and affection of E.M. Forster made me understand why even democracy deserves only two cheers—three being reserved for the holiness of the heart's affections. His love of children was so great that when I took a few of my younger visitors to him, he spent hours fussing over them.

The Post-War World

The post-war world and its problems did influence our learning of international economics—but again primarily through the debates on the post-war architecture of international economic co-operation which was then on the drawing boards at Brettonwoods.[9] We knew all about the Keynes and White Plans. If the British were interested

in post-war reconstruction aid and some scope for controls and discrimination for them, we were interested in development aid and the scope for controls and discrimination for developing countries. Above all, during the Anglo-American loan negotiations, we were interested in safeguarding our sterling balances.

On his return after negotiating the Anglo-American loan, Keynes gave a talk at the Political Economy Club where I asked him what the loan agreement truly intended for the release of sterling balances. There were contradictory indications in the loan agreement—at one point, the agreement spoke of the loan being necessary to enable the UK to honour its war-time obligations and at another, it said that if in difficulty, the UK should honour its obligation to repay the US loan first and then its other obligations. Professor Robertson intervened to say that he had the same question. This gave Keynes a perfect way out: 'Dennis, I can understand I.G. asking that question. But I am surprised that you, who used to always find words which could satisfy all points of view at Brettonwoods, are now telling me that I am so incompetent without you that even young I.G. can find me out.' The answer was clear.

Another example of Keynes's acerbic style came in a lecture he gave at the Marshall Library where he referred to a talk he had recently given at the Federal Reserve Bank in Washington, D.C. He had insisted that, in view of his poor health, only Federal Reserve economists should be invited. But he found the room packed and was told they were all Federal Reserve economists. At this point, Mrs Robinson and Kaldor laughed, and Keynes came down on them like a ton of bricks: 'Nicky, Joan, do not laugh. We think we have done our job if we produce one or two great economists in a generation. The Americans believe in creating scores of good economists and technicians in a generation; and that is why they succeed economically, and we do not.'

It is interesting to recall how theory is often invented to serve national interests. The left in the UK believed that after the war the UK

would need import and exchange controls and the right to discriminate against dollar imports if it were to survive US competition. The theory of a permanent dollar shortage was invented, in particular, by Mrs Robinson. The argument was that since the US had taken the lead in technology over practically the whole range of economic activity, including industry, agriculture and services, and since technological progress there was more rapid than in other industrialized countries, it would have continuing comparative advantage over a whole range of international exchange. This would be reflected in US wages being low in relation to their productivity as it would take time for wages to adjust to rapidly rising productivity. The US then would have an unfair advantage which had to be counteracted by controls and discrimination against dollar imports. The US obviously was opposed to this.

I was suspicious of the permanent dollar shortage argument as it reminded me of arguments for protection against Japanese goods. It was often argued that wages in Japan were 'unfairly' low over a large range and were likely to remain so as it takes time for wages to adjust when productivity is rising rapidly in countries which are simply catching up. The parallel to what might be argued against India was obvious. This was one reason for the thesis topic I chose, and I had arguments with Richard Kahn and Mrs Robinson on why there was nothing unfair about wages lagging behind productivity when there was structural unemployment: the choice was between higher wages for a few employed or more employment in the aggregate. This point still needs to be driven home in the national as well as the international context.[10]

But I suspect we had some sympathy with the permanent balance of payments difficulty syndrome even if none with the unfairness of low or laggard wages. In years to come, we developed sophisticated arguments for long-term protection and quantitative import restrictions for developing countries. The two-gap theory was not an invention of Hollis Chenery; he may have formalized it. Mrs Robinson—who else—distinguished between the inflation gap and the balance of payments gap in her *Accumulation of Capital*, which appeared in 1956.[11] I had developed the same argument in a seminar at Harvard in 1960 and in a Conference of the International Economic Association in September 1961 at Brissago.[12]

The major impact of the war on post-war economic thinking and policy came towards the end of the war and with the installation of the new Labour government in 1945. The publication of the Beveridge Report on Employment and Social Security and the passing of Employment Acts in both the UK and the US were landmarks on the way to fine-tuning in macro-management and better distribution of income or greater equity or social justice and individual security through the enactment of the welfare system. If the war demanded supreme sacrifices from everyone, the post-war world had to ensure minimum rights to everyone, not just to life and liberty but also to a decent and secure livelihood through a network of welfare measures including access to education, health facilities, sickness and unemployment benefits and indeed active promotion of full employment. It was not Soviet Communism but American liberalism and British Labour which were the foundation stones for our views on economic policy. I was particularly impressed by the GI Bill of America which gave every young American who had taken part in the war effort two years of paid leisure to do what he liked at an age when it counts most—to study, to travel, to set up a business or just to roam the streets of Paris, Rome or Mexico.

The war and the thinking about the post-war world created a new faith in the need and the efficacy of extensive governmental intervention in economic life. Even the aversion to controls based on Indian experience vanished in the presence of the orderly and by and large efficient administration and willing acceptance of controls in Britain, not just during the war but also during the years of post-war austerity. It was easy to believe then that governments could be honest, well-meaning, dedicated to public purpose and intelligent enough to pursue public interest wisely and that people would give them willing co-operation. It was Attlee who had said that the art of politics lay in making people accept current sacrifices for a better tomorrow. What could be believed about Attlee and the other Labour leaders could surely be believed

about Gandhiji and Patel and Nehru. We did not know then that politics could degenerate into a self-serving and cancerous game of trying to please everyone in the present by making them oblivious of the future.

Economics of Development

I do not know at what point in my training as an economist we began to divide economics into four inter-related but distinct parts: (a) Micro-economics or the allocation of a given amount of resources more or less fully in use; (b) Short-term macroeconomic management or fluctuations in incomes, prices and employment when resources and technology are given but not always in full use; (c) Economics of growth or development when technology can improve and resources can grow (we did not emphasize then that resources can change for better or for worse); and, (d) Economics of distribution. By the time I graduated at Cambridge in 1946, we knew a good deal about macroeconomics and distribution of income, but little of economics of development. As already mentioned, microeconomics tended to disappear from our sights. It is surprising that 'development', that is, the *Wealth of Nations*, which was the soul and substance of classical economics found little mention in the classroom then. No one read Adam Smith or J. S. Mill or even Marshall—Keyneseana conquered all. But for someone from India, it was natural to think of development. I was also aware of the fact that international trade too had received scant attention in what we were taught and what we read.

It was to repair these omissions that I thought vaguely of working on economic development and international trade for my thesis. As more and more countries industrialize, does the scope for international trade get reduced? Can international trade be the engine of development? How does the industrialization of new countries like Japan or India impact on the well-being of those already industrialized? Can there be a more or less permanent flow of capital from the rich to the poor? What sets the limits to growth? I raised these and related questions, but alas, was not assiduous or ingenious enough to answer them adequately.

Problems of development had begun to surface in current economic literature by 1947–8, but there was nothing like what one might call a General Theory of Economic Growth. Nor was there a clear link between microeconomics and macroeconomics or between the latter and a theory of development. Distribution was always a by-product, traditionally of microeconomics, but more recently also of macroeconomic factors. Increasingly, it began to be seen as exogenous or the result of deliberate policy. Seeking equity as well as efficiency through the working of markets was not fashionable then. We were more obsessed by imperfections than bewitched or beguiled by notions of perfection—as perhaps we are even now, at least from time to time.

Harrod's *Towards a Dynamic Economics* did break a new path. But the popular version of the Harrod–Domar formula seemed to me then a tautology which did not say much. Mrs Robinson's stricture against the Quantity Theory of Money, 'It is telling us nothing, we are telling it', applied to the Harrod–Domar formula too. It focused attention exclusively on the rate of savings and investment and the need to increase the latter by increasing the former: investment opportunities in poor countries were obviously unlimited. But is the capital–output ratio really constant or is the main task of development really to improve this ratio—which is only another word or capsule for over-all productivity? If one had asked how productivity can be increased rather than how supply of factors can be increased, one might have come to a different and perhaps more relevant recipe for action. It would have drawn attention to allocative efficiency, importance of motivation and incentives, institutional arrangements including property rights, educational standards of workers, social emulation, habits of co-operation and many such 'supply side' factors. The emphasis instead was largely on savings, that is, thrift and sacrifice. One could have argued—as was later argued about Japan and the East Asian countries—that high rates of growth did not result from high rates of savings, but the other way round. When incomes grow rapidly, it takes time for consumption standards to be revised fast enough so that savings rates rise. What makes incomes grow is

rise in productivity which is the outcome of a variety of societal and institutional factors. In this sense, the savings–investment enthusiasts shunted off the train on the wrong tracks—from productivity or real developmental or supply-side economics to emphasis on augmenting factors of production, and that too narrowly on capital.[13] The macroeconomic habits of aggregation made us oblivious of the fact that capital formation also has to be of the efficient kind— appropriate composition, appropriate quality. With the help of foreign aid, we built up a lot of capital, but often of the wrong kind and of poor quality. If we had set about obtaining our capital goods as fully paid items on the basis of our own export earnings and given greater attention to exports, I reckon India would have developed faster and better; and we would have had a more favourable capital–output ratio as well as a higher savings ratio!

Be that as it may, as an operational model or prescription, the Harrod–Domar equation was of little value and may well have misled. During my student days, there were glimpses also of other development models. The two that appealed most were of 'The Big Push' variety. Rosenstein-Rodan's classic piece based on his study of the development needs of south-eastern Europe argued for simultaneous development on a broad front as did Ragnar Nurkse's on the basis of generating sufficient demand to realize economies of scale inherent in complementarity. I do not recall the argument well. But it fell well on fertile minds: we were all for a big push and industrialization on a broad front. The shades of Nehru and the Bombay Plan were there, as was the belief that the West had taken the lead over us as a result of industrialization. The infant industry argument—and learning by doing could, we assumed, be writ large and extended to the whole spectrum of industries and not just a few.

My research on Japan and Australia had also led to the view that ultimately all rich countries have a broad-based economic structure in which technically advanced industry as well as agriculture appear. If that is the ultimate profile of economic arrival, why not march towards it also on a broad front, unless there are

good reasons for some alternate approach? Somehow, without any conscious bias against exports, it was felt that international trade could not be the main engine for economic growth. It was not just the fear of restrictions by the rich—although that existed as exemplified by the experience of Japan. The central idea was also that you needed to infuse modernity, technological change and efficiency all along the line and not in just a few export industries. All this was not fully articulated or understood. But it was deeply felt.

I remember a meeting of the Indian Majlis[14] in Cambridge on 15 August 1947. We were all deeply depressed by Partition and the communal riots and the impending break-up of the Majlis itself. We decided to meet for the last time as 'a whole' and discuss our role after independence. One and all, we articulated visions of rapidly catching up with the best in the world, economically, technically and intellectually. We were not to be left behind in any respect for long—and we would try and play our part by being world-class engineers and scientists and even economists. It was not Antyodaya or the poorest and most deprived Indian that stood before us then. It was Nehruvian grandeur—India marching shoulder to shoulder with the richest and the most powerful in the world with its head held high—that excited us. A vision to be imposed from above—not an upsurge for the uplift of the submerged from below. It is certainly arguable that a long-term vision was as necessary as the elementary duty to the poor in the present that we failed to emphasize. If both are necessary, they have to be consciously remembered, reckoned with and reconciled. But economic development—let it be admitted—was seen then by most of us as a political statement and not an expression of our compassion or of our humane and liberal instincts. Those existed. But we assumed they would be taken care of anyway—by growth itself and by some version of the welfare state.

I recall with some satisfaction that my study of Japan for my thesis led me to emphasize social or cultural factors in development. Why was Japan so successful? It was not easy to explain. It could not be that Japan was not colonized. Neither was Thailand.

Why were Japanese savings rates high and its propensity to import low, which facilitated growth? Why was Japanese labour ready to adjust and cooperate rather than agitate? It could not be coercion or compulsion: coercive regimes were dime a dozen then. Japan—may be because of its geographical insularity—had developed certain national traits which included readiness to emulate as entrepreneurs but reluctance to copy as consumers or workers or employers. Work habits and consumption remained culture specific. Nowadays, it is not politically correct to speak of national or group characteristics. But they do exist. They are not a reflection of national character; and characterization such as 'good or bad', 'violent or peaceful', 'honest or dishonest', or 'rational or superstitious', which imply judgement and condemnation if not contempt, are as off the mark in truth as they are self-serving in practice. But as an imprint of one's own unique history, national traits are a reality, transitory and changeable as they may be. We may all share some human traits. But we differ in our experience which moulds different patterns of reaction; and some of these are creative and some are not. The liberal instinct to shy away from explanations in terms of national traits is understandable, given the human tendency to judge. But an explanation has to be as objective and honest as it can be, even if it must eschew judgements of virtue or vice. We in India can certainly gain by more introspection about our history and about the present state of our national culture.

I have a vague recollection that some of Kalecki's writings also influenced our vision of economic development. His view that the average degree of monopoly in the economy determined the relative share of wages and profits in national income and as a consequence the level of aggregate demand (because workers and profit earners have different propensities to save) certainly provided a sort of link between microeconomics and macroeconomics. But I think Kalecki also linked the capacity to invest with the capacity to meet the demand for wage-goods if inflation or balance payments difficulties were to be avoided—thus giving another insight into development, viz. the need for balance between the level of investment and the supply of consumer goods. Or, I am perhaps attributing to Kalecki what Kaldor later developed more fully in a lecture he gave in China. But in any event, one of the ways in which Keynesianism

influenced thinking on development was by emphasizing more than one link between investment and consumption: via the lack of it, that is, and also by the supply of its ingredients.

In short, by the time I completed my studies at Cambridge in 1949, I had a great deal of exposure to ideas on development and on economic policy. What it lacked in precision or analytical rigour, it made up to some extent by the scale of its canvas which, if not as large as that of the classics, was a bit larger than that of many present-day students. At any rate, it was based as much on a reading of economic history as of economic theory—and both readings were guided by a nationalist vision.

Harvard

The year (1947–8) I spent at Harvard while working on my thesis was rather uneventful from the point of view of my economic training. I was by then too anxiously involved in the nitty-gritty of my thesis; and the Widner library provided ample scope for poring over the available literature on international economics and on Japan, Australia and Argentina which constituted the case studies for my examination of the interaction between international trade and economic development. Even Widner had little then on what may be called New Development Economics.

As for teaching at Harvard—which I only sampled as I pleased—much of it was not inspiring as it was a repetition of what I had learnt at Cambridge about Keynesian economics. Even Chamberlin on monopolistic competition was rather tedious. Haberler, while being very helpful to me as my 'adviser', was not a brilliant lecturer. Leontief brought something new through 'input–output' analysis. But the star performance was by Schumpeter. He gave a course on what he called 'Economic Models'. It was in fact a course on History of Economic Thought centred on the idea that each theory was a model of the circumstances of the time—and none was better than the other, but only more relevant. Later, Professor A.K. Dasgupta was to expound the same idea in his own inimitable way in his *Epochs of Economic Theory*.

Samuelson's article on 'Factor-Price Equalization' had already appeared and had heralded his arrival on the economic scene. But my attempt to attend his lectures on Mathematical Economics at the MIT came to naught: he did not give that course that year. The dominance of US universities in economics was already under way; but it had not yet arrived with a bang. But some of the future stars like Tom Schelling, Carl Kaysen, Robert Dorfman—and, indeed, Harry Johnson, also with me at Cambridge—were around at Cambridge, Massachusetts, when I was there. Having had a Harvard connection in my early life had a rich payoff in my later years.

The most memorable event of the year at Harvard was the spontaneous reaction of ordinary Americans to the assassination of Gandhiji. For weeks after that shameful episode in our national life, I was stopped in the street by ordinary people who wanted to tell an Indian about their sense of deep personal loss and their feeling that the world had lost its most remarkable thinker and leader.

*Baroda**

The nine months I spent at the University in Baroda (1949–50) between Cambridge and the International Monetary Fund witnessed little excitement about economic policy in myself—or I suspect in the country at large. The scars of Partition and the memories of the Bengal famine overshadowed everything. Refugee rehabilitation, consolidation of communal peace after the assassination of Gandhiji and some blueprints of river valley developments along the lines of the Tennessee Valley Authority occupied the attention at the Centre; and the states had to grapple with essential supplies. The need for a US wheat loan was the first foray in foreign aid and the frustrations and friction it causes. Panditji was incensed by some criticism of India in the US Congress and was prepared to buy the wheat. As usual, wiser counsels prevailed and a wheat loan—I believe of $190 million—was negotiated.

*Washington, D.C., 10 December, 1999.

The only notable economic event I remember is the devaluation of £ sterling in September 1949 and India's decision to follow suit. Pakistan did not. But I remember no major controversy about India's decision—or for that matter, of the UK's decision, despite the devaluation it implied of our sterling balances. I gave a talk on the Baroda station of All India Radio defending both decisions—which C.D. Deshmukh listened to and liked (as I learnt from my friend K.N. Raj who worked with him then). On ideas about economic development too, there was little stir. At the annual conference of the Indian Economic Association at Waltair in December 1949, I gave a talk on the extension of the Keynesian framework to problems of development—a sort of pot pourri of my ideas then. Delivered extempore at breakneck speed, it has blown away even from my memory—although the speed, if not the substance, elicited some admiration from the delegates!

International Monetary Fund

The four years (1950–4) I spent as economist and assistant chief in the Financial Problems and Policies Division of the Research Department in the IMF rounded off most effectively my training as an economist destined to be an economic adviser. In endorsing my candidature to the Fund, C.D. Deshmukh, who was Governor for India on the Fund's Board of Governors, had emphasized the need to train young Indians to handle the problems of the Indian economy and the role that the Fund could play in such training. E.M. Bernstein, who actually selected me, made it clear at my first meeting that his job was to train me to be a practical economist and then pack me off to India. Nothing suited me better. Bernstein did exactly that. He even took me with him—contrary to normal Fund practice then—on a Fund Mission to India in 1953 so that I could see how things were first-hand before I made a commitment to return. When the chance for that came in 1954, he on his own insisted that I go on leave for one year so that I could return to the Fund if I did not like the atmosphere in the Government of India. The affection I received from the Bernsteins and the debt I owe to him are among my happiest memories.[15]

The Fund and its policies and my happy memories of those days are not within the scope of this enterprise. But I must acknowledge the training I received then and how my views on economic policy evolved. There could not be better teachers than E.M. Bernstein or J.J. Polak or Marcus Fleming (who came later) and better colleagues from whom one learnt much than Henry Murphy (monetary expert), Richard Goode (fiscal expert) or Bill White (Harry White's nephew and a good theorist who was with me at Harvard) or Sidney Alexander who had taught me statistics at Harvard. With others like Irving Friedman, the relationship turned into a life-long friendship.

It was in the Fund that I learnt how to read budgets and balance sheets of Central Banks, how to use national accounts, how to work out intricate correlations (e.g. in working out the income and price elasticity of demand for gold in India,[16]) how to look at an economy as a whole or analyse and interpret economic events. We were dealing with real economic events, using data, much of it currently developed at the Fund (e.g. on balance of payments), and looking at life as it currently unfolded and as it evolved over time.

A list of my assignments would illustrate the range of the training. The first assignment was to work out the elasticities of demand for gold in India. The idea was to explain why gold prices had not risen in India after the 1949 devaluation. This was followed by an analysis of post-war monetary policy in Europe, of selective credit controls[17] in Latin America, of the phenomena of the 'stabilization crisis' (i.e., why an attempt to control inflation which has lasted long often leads to a sharp and somewhat excessive drop in incomes and employment), incentives for savings, and taxation and economic development. There were also studies on various aspects of a problem, particularly the gold problem (i.e. purchase and sale of gold at prices different from the official price of $35 an ounce) and involvement in economic evaluation of countries as diverse as Thailand and Paraguay.

Admittedly, the focus of the Fund was rather narrow. Some of us from developing countries used to say rather mockingly and irreverantly that there were two kinds of economists: the balance of payments economists and economists and that the Fund had many of the former but only a few of the latter. The next door neighbour, the World Bank, was supposed to deal with development.[18] But what the Fund did, it did well.

The Fund had little by way of dealings with India then. Even as regards advice, it was C.D. Deshmukh who took the initiative to seek it. He invited Bernstein specifically, not the Fund; and the advice was not about balance of payments or import restrictions but about 'Economic Development with Stability', the title of the Mission Report in 1953. What it says about development is and was general knowledge, for example, the importance of education. But about the scope of 'safe' deficit financing, it was explicit and showed how one analysed changes in money supply. The focus was on monetary analysis and not on national income accounting although the language of the latter might have been used. I am afraid this dichotomy remained in India for many years and is perhaps even now operationally in existence. The absence of timely national income statistics is one reason. But the ease of money supply analysis is only one reason for its primacy. Many like Bernstein were essentially monetarists in practice even though they became Keynesians in theory. But Bernstein went much deeper than most in the article on 'Inflation and Economic Development' which was written soon after we returned from the Mission.[19]

One can explain inflation in many ways: as a result of excessive creation of money, as a manifestation of excess demand originating from a budget deficit or a balance of payments surplus or an upsurge in private investment or private consumption, or as a result of the wage–price spiral or of supply of consumer or wage goods being inadequate in relation to the level of investment. But none of these approaches explains what lies behind these phenomena. Bernstein points to the one common factor behind all these: the struggle of one section of the society to claim a higher share of national income than what other sections are willing to surrender without a fight. Inflation—or monetary expansion or excess demand or the wage–price spiral—are the result or manifestation of this social tug of war. This, I think, is a profound insight. It says

that you cannot exorcise Marx from markets. Not all the pulls that are exercised on the market come from money power. There are other power struggles and inflation is the result of the failure to settle these struggles amicably. There is as much politics in inflation as economics; and it needs politics as well as economics to bring inflation under control or to avoid it. And that goes for moderating growth in money supply or reducing budgetary deficits or ending a wage–price spiral—if we want to focus on symptoms rather than on the underlying malady.

Endnotes

1. As Executive Director for India at a board meeting of the IMF in 1961 when a drawing by India was approved.
2. Please see Appendix I for an elaboration of this.
3. *India's Teeming Millions,* Gyan Chand, London, George Allen and Unwin Ltd., 1939.
4. It was the only passport available in the Resident's office and had several pages torn, which required much explanation at many immigration counters.
5. A big truck full of boxes and blankets arrived later, but a suitcase full of clothes and personal effects was stolen. All I got by way of compensation—I had not insured my luggage as I thought insurance subsidized the careless at the expense of the careful—was a letter from the shipping company that 'however painful (my) experience, it reflected in no way on the efficiency or integrity of British business in normal times.' British labour, obviously, was another matter.
6. Nevertheless, it was during the war that 'operational research' developed as an extension of the marginal theory in economics. After the war, Professor P.M.S. Blackett gave the Marshall Lectures in which he outlined how the economists were the first in his war-time team to find an answer, by using marginal analysis, to intricate questions like the configuration of attacking fighter planes or the stock-piling of essential supplies. The scientists carried the approach much further.
7. Everyone was given a certain number of points or coupons; and each item of consumption could be had by surrendering a certain number of points (as well as a certain amount of money). You could take your decisions only with reference to the 'price' in terms of the number of points required because you would still be left with money when all your points or coupons were used up. Thus only the points-income and point-prices were relevant.

8. I spent the year 1947–8—sandwiched between my third and my final year at Cambridge—at Harvard where I was awarded a research fellowship.
9. The famous Bretton woods conference in the US that gave birth to the World Bank and the IMF.
10. I had a similar argument with Maurice Dobb about the alleged superiority of communism where public ownership meant that old equipment will not be scrapped until new equipment could produce the same goods at a lower average cost than the marginal cost with the old equipment. I had argued that by the same token, we must agree that in a capitalist economy, monopoly was better than competition. Somehow, the equation of communism with monopoly did not square well with his leftist convictions!
11. *The Accumulation of Capital,* Joan Robinson, London, Macmillan and Co. Ltd, 1956.
12. 'Trade and Payments Policy for a Developing Economy' by I.G.Patel in the conference volume entitled *International Trade Theory in a Developing World,* edited by Roy Harrod and D.C. Hague, London, Macmillan and Co Ltd, 1963.
13. More savings and more investment are obviously necessary. But other things are even more so.
14. An association of students at Cambridge from India as it was before partition and Sri Lanka.
15. This affection continued long after both of us left the Fund. In 1977, when his successor Polak retired as Director of Research at the IMF, Bernstein wanted me to succeed Polak—but he understood why I preferred to return to India from the UNDP to be Governor of the RBI. When I was at the LSE, he donated a set of his newsletters to the LSE library, carrying them in a suitcase from his hotel in Russell Square to my rooms at the LSE.
16. There were no national income data for India over the years. Polak suggested I use sugar consumption as a substitute as the income elasticity of demand for sugar in Indonesia was found to be unity! He also taught me how negative figures in a series could be converted into positive ones. I was very sceptical of all this and had a simple diagrammatic explanation of why the price of gold in India did not rise after the 1949 devaluation. But the correlation confirmed Bernstein's judgement that both the price and income elasticity for demand for gold in India were high.

17. My papers on post-war monetary policy and selective credit controls were published in the IMF Staff Papers. Polak was very keen on publishing the paper on the elasticity of demand for gold in India; but I resisted this as, unlike him, I was sceptical of the correlation analysis.
18. Not that one saw much evidence of that in the early 1950s. About the only thing the World Bank did then which interested us was its part in the settlement of the Indus water dispute—alas, with no sequel in the subcontinent.
19. This article was published in the IMF Staff Papers under our joint authorship. But I have always acknowledged that the core thinking was done by Bernstein. More evidence of his generosity.

2

Deputy Economic Adviser 1954–8

In May 1954, I returned to India to become the Deputy Economic Adviser in the Ministry of Finance, Department of Economic Affairs, at the invitation of J.J. Anjaria who was the Chief Economic Adviser.* Anjaria was my examiner at the B.A. (Honours) examination in India and had been generous in marking my paper. I also attended his lectures on Economic Theory at the Bombay School of Economics for a couple of months in 1944. He had had a brilliant career at the LSE and was one of the most lucid expositors of economics I have ever known. To his knowledge of economics and invincible style, he added a most transparent and generous disposition with an ability to command respect from young and old. No one could doubt his commitment to whatever he did; and he inspired by his own untiring example. My generation of economists owes a great debt of gratitude to him for paving the way for acceptance and even appreciation of economists in Government service.

The Deshmukh Years

The new 'Economic Division' in the Ministry was the creation of C.D. Deshmukh, the Finance Minister, who had supervised the

* New York, 21 December 1999.

creation of a strong Research Department in the Reserve Bank when he was the Governor. Deshmukh knew the importance of economists and economic advice. Another economic division was created in the Planning Commission—also under the leadership of Anjaria. Two other older economic set ups existed in Delhi then—in the Ministry of Commerce and Industry and in the Food and Agriculture Ministry. These older divisions were soon overshadowed by those that were the creation of the all-powerful Finance Minister. Deshmukh felt that the supremacy of the economists in the Finance Ministry led to better coordination of economic policy—an aspect in which there could be success only when the Finance Ministry had a strong Minister or a Secretary respected by his peers as was the case in those early years. Deshmukh also opposed the creation of economic divisions in other Ministries, particularly the Labour Ministry and insisted that I should also be their adviser, something which I neither liked nor supported. Eventually, this whole structure of Finance Ministry paternalism came down on its own weight.

Any history of economic policy in India must trace the proliferation of economic advice in Delhi—a process in which our division acted as a nursery. Many economists trained in the Ministry of Finance[1] went on to hold important positions in other ministries. And it was this presence of like-minded friends in several ministries which provided the communication and coordination of views and advice that existed despite departmental jealousies and rivalries, not to speak of jurisdictional separatism. Let it also be said that very confident and economically literate civil servants who belonged to the economic and finance pool were also an important and integral part of that process. In the fifties and early sixties, there was some coherence in economic policy and much inter-ministerial cooperation in its formulation as well as implementation. Among the ministers, the credit for this, apart from Pandit Nehru, must go largely to T.T. Krishnamachari (T.T.K.) and Morarji Desai, the former by active involvement, and the latter by benign but discerning trust. Deshmukh was a loner and perhaps not so secure of his position in the Government. It is difficult for many now to appreciate the wonderful trust, regard and even affection that existed in the early years among economic ministers, civil servants and experts.

During my first year in the Ministry, I was far removed from the making of economic policy. Anjaria had his office in the Rashtrapati Bhavan Annexe. The rest of the Economic Division was quartered in the war-time abomination built on Raisina Road, known as P Block. I was a sort of 'mukaddam' or supervisor of this staff as Anjaria's deputy—running the day-to-day administration, organizing day-to-day work such as preparing answers to Parliament Questions or briefs on a variety of matters and to some extent moulding a team of young researchers. The hub of the ministry, including the office of the Finance Minister, was in the North Block. This physical separation spoke of our subaltern role. All this was to change with the arrival of T.T.K. (in 1956) and even earlier with the preparation of the Second Plan.

My first encounter with Deshmukh was disconcerting. At that time there was much controversy about whether we should go in for a substantial increase in steel production. No less a person than Sir Arthur Lewis had argued that India had a comparative advantage in steel production and should aim soon to increase steel production from one million to ten million tons, much of it for export. As Minister of Industry, T.T.K. had taken up this theme and wanted to set up three new steel plants to raise steel production to 4–6 million tons in the first instance. This was not absurd in my eyes at least; after all, as early as in the thirties India's private steel industry was more efficient than that of Japan. But Deshmukh ridiculed the idea in my first meeting with him, 'Those people do not know what steel is and where it can be used. I have asked them to tell me how much of each variety of steel they want produced and where and in what quantity each variety would be consumed. It would take them months to answer these queries. And in the meanwhile, the whole thing will be forgotten.' I was shocked as

much by the shades of bureaucratism as by the lack of foresight. I narrate this to underline that Mahalanobis was not without predecessors at least in one important respect.

I suspect the primary attention in economic policy in 1954–5 was devoted to completing the First Plan without inflation and serious dent on sterling balances—in both of which it succeeded. But the impression was gathering that the First Plan was too modest and we needed something bolder in the Second Plan.

Looking back, the one significant event of the time was the nationalization of the Imperial Bank which thus became the State Bank of India. But the inspiration for this came from no socialist doctrine. It was the more humdrum concern for extending bank credit to the rural areas and small industry—something much talked of even in the thirties and forties. It was D.R. Gadgil—one of Deshmukh's closest friends—who had authored a Report on Rural Credit (commissioned by the Reserve Bank, not the Government) in which the suggestion to nationalize the Imperial Bank was made and Deshmukh rightly decided to implement it expeditiously. Let it be also said that H.M. Patel, Finance Secretary at the time, worked ably and tirelessly to make the transition a smooth one. No less a person than the previous Finance Minister, John Mathai, agreed to be the first Chairman of the State Bank. Here was another example of how patriotism inspired ministers, civil servants and economists alike at the time.

Yet another experience of the spirit of the times came on Independence Day in August 1954 when I received an invitation to dine at Panditji's residence the same evening. I thought the invitation must be for H.M. Patel. But I was assured that it was I, a mere deputy economic adviser of two or three months standing, who was summoned. There were only seven or eight guests at the dinner. Panditji pointed to one of them—the young Maharaja of Udaipur—and explained to me that I was invited so that the Maharaja could have someone of his age to talk to. 'These princely people have to change and come to terms with the changing world. The Udaipur rulers had vowed never to enter Delhi alive as long as India was under foreign rule. I have been inviting this young man to come now that we are free, and he came for the Independence Day ceremonies this morning. Please talk to him and tell him something about the world outside.' That the Prime Minister of India should have heard of me, that he should be so solicitous about the young prince and that he should be so completely free from any sense of rank or protocol or status simply swept me off my feet. After that, it was simply a matter of great pride to work for him and for all that he stood for. Such was the climate in the dawn of Independence.[2]

My first assignment as Deputy Economic Adviser was to organize a complete set of statistics on the Indian economy. Deshmukh was to attend the annual meeting of the Bank and the Fund in Washington in September 1954 and was to visit other countries as well. Unlike other ministers I knew, he drafted most of his speeches and wanted all facts on India at hand. We worked hard on this project and prepared a set of tables on everything from population to foreign trade and four fat albums were the result. There could not have been a better preparation for an economic adviser than this exercise. It made us look at everything and judge the reliability of the sources, and gave us an idea of the orders of magnitude in Indian economic reality. Without a proper grasp of statistics—and evolution of the right kind of statistics—there could be no economic advice. And when advice has to be offered often on the run so to speak, it helps to have the facts and the orders of magnitude firmly fixed in mind. Any story of economic policy in India must narrate not only the involvement of economists and civil servants or ministers; it must also have a chapter on the contribution of statisticians.

In the Economic Division itself, this first exercise led to many refinements and regular publication of handbooks which helped the preparation of the Economic Survey when it came to be published regularly a few days before the Budget. We also tried to develop an economic classification of the Budget. While our primary effort helped the Central Statistical Organisation in its analysis of Government finances, I am afraid I cannot claim that our work on economic classification had much impact on budget-

making or economic policy in general. The same can be said about other attempts at sophistication made or recommended from time to time—such as zero-base budgeting or accounting or shadow-pricing for project selection and the like. While sound in theory, such sophistication is not easy to be operationally translated and remains essentially in the realm of rhetoric. At best, it provides qualitative justification for such policy changes as are obviously necessary or as are otherwise fancied by the politicians. Economic classification of past budgets might show a trend which needs to be corrected even if one cannot say on the basis of forecasting models by how much. And one argues for changes in interest rates or exchange rates on the basis of known facts such as inflation or balance of payments difficulties, without working out appropriate shadow rates. Theory then often points only to a direction, seldom to a quantitative target.

Surveys, speeches, monographs prepared for important conferences and even answers to parliament questions are often more effective channels for advice on economic policy than notes or studies prepared on specific issues. The latter are important. But in real life, when a problem arises and needs to be tackled, there is seldom time to prepare a well-rounded research paper to tell us what needs to be done. One relies on research already available and general impressions one has about what is wrong and what might work—and these are often conveyed informally through surveys, speeches and the like. Once a minister has read out a speech written by you, he owns it. Once a department submits something to a conference, it recollects, formulates and commits. Our learning process in the early years in the Ministry was through all such devices.

An interesting conference I attended then was held in Simla to consider the possibility of some kind of a 'Marshall Plan' arrangement for South and South-east Asia.* Under President Truman's

*New York, 22 December 1999.

'Point Four Plan', a beginning had been made with US technical assistance to developing countries. Such assistance was given a multilateral face under the Colombo Plan of which Canada, Australia, the UK and several others were 'donor' members. Given the success of the Marshall Plan and perhaps as an extension of the SEATO (South-east Asia Treaty Organisation) born out of the exigencies of the incipient Cold War, the idea was mooted—by the Ford Foundation I think, under US inspiration—that the South and South-east Asian countries could themselves come together, define their needs, and get a joint allocation of aid which they could largely administer. The Simla Conference was to explore and indeed advocate the idea. C.V. Narasimhan, Joint Secretary in charge of the subject in the ministry of Finance, was in favour of the idea and had obtained the brief to support it.

I was included in the delegation at the last minute and I read the papers after reaching Simla. I thought any such joint arrangement would result in inaction or unfairness to India as we would be asked to behave generously as an elder brother and as Pakistan, in particular, would adopt negative tactics till it got much more than its share. P.C. Bhattacharya who was to be the leader of the Indian delegation also saw the brief in Simla and agreed with my point of view. To my surprise, H.M. Patel, the senior-most secretary, decided to disregard the brief and support our idea. But how was this to be done since our position was known at least to some of the delegates? Either Bhattacharya or Patel found the answer. Patel was to chair the conference. He should ask Pakistan to speak first. Knowing the Indian position, Pakistan delegation would raise difficulties and objections even if they did not show active opposition. At that point, Bhattacharya should say on behalf of India that in view of Pakistan's strong feelings, the idea was not worth pursuing. Things went exactly as planned—and the conference and the idea were still-born.

Looking back, I am not sure if our stand was right. Perhaps that particular ship would have sunk sooner or later, given Pakistan's intransigence and the development of the Cold War. But within a framework of South and South-East Asian Marshall

Plan, our later efforts to mobilize foreign aid might have been facilitated. And who knows—there could have been sequels to the Indus Water Treaty at least in relation to Nepal and others.

Deshmukh left the Ministry in 1956 in protest against the exclusion of Bombay from the state of Maharashtra. I still feel this was an excuse for leaving a post in which he was feeling increasingly uncomfortable. He had gone along with the draft Second Plan framework, partly out of regard for Mahalanobis who was a friend from their Cambridge days. But I am not sure he relished the idea of implementing it. There was also too much of sniping from the wings—particularly from T.T.K. who succeeded him—and Deshmukh was not all that sure that Panditji would always support him. The Congress Party had begun its verbal flirtations with socialism,[3] and I cannot believe this was much to Deshmukh's liking. In any event, T.T.K. stormed into the North Block and life changed, particularly for the economists. He was fond of Anjaria and gave him a room next to his. He had also heard of me—and I moved to North Block on the ground floor just opposite the lift at the entrance. But before writing about the T.T.K. era, I must refresh my memory about the Second Five Year Plan which had already taken shape and indeed was accepted in principle for implementation by the time T.T.K. came to the Ministry of Finance.

The Second Five Year Plan

Once the initial herculean task of removing, if ever one can altogether, the scars of partition and communal carnage, refugee rehabilitation, smooth transition to a national administration and integration of Princely India was completed by 1950, attention turned to rebuilding the nation through planned development. India's First FiveYear Plan began in 1951 although the final plan document was not ready for another two years. It has been said that the First Five Year Plan is like the Mahabharat: there is nothing in the Indian economy which does not find a reflection in the Plan and there is nothing in the Plan which is also not found in Indian reality. It was natural that the first exercise in planned development

should be a sort of reconnaissance trip: surveying and mapping out of the entire terrain so as to understand it better. Such a comprehensive exercise was bound to be eclectic and even discursive and to some extent tentative and cautious. But in the hands of practical men who shaped the plan, it contains much wisdom that is still relevant. Some things that required to be done were obvious. The memory of the Bengal Famine, the dislocation of the Punjab peasantry and the early shortages of food emphasized the need for increasing food production. Hence the emphasis on irrigation, large river-valley projects, community development and the production of fertilizers. The Plan, which was really a programme of public expenditure, reflected this as well as the entire gamut of national aspirations. Modest as it was, it achieved what it set out to do, and without much inflation or dent on sterling balances—two major concerns then. Those accustomed to think of India as a wounded civilization or an economic laggard or a classic underachiever would do well to refresh their memories about the first turbulent and triumphant decade after Independence when so much was achieved and so much overcome, so much so well articulated and so well begun. That much we owe to the memory of Gandhiji, Patel, Nehru and the thousands who worked in various capacities in the corridors of power in Delhi and in the states at the time.

Thinking on the Second Plan had begun seriously by the beginning of 1955. My memory of its conception goes back to a meeting of the panel of economists when all the good and the great—and some not so bright and beautiful—in the Indian economic firmament were present. I have the impression that there was a general consensus on a number of points: the Second Plan should be bigger and bolder; it should aim to accelerate the rate of investment and the rate of growth; this should be done without inflation; while agriculture deserved continued attention, greater emphasis should be put on industrialization; production of steel and fertilizers should be increased substantially; the plan must generate employment on an adequate scale; and the equity or distributional aspects should not be overlooked. I emphasize this to underscore that the Plan or the thinking on the Plan then was

broad-based and by no means confined to some narrow dogma or model. If there were differences of opinion, there was also agreement over a considerable range of issues. It is also significant that neither socialism nor foreign aid figured much in these early economic discussions. The former entered through the political door;[4] and the latter was the child of necessity.

D.R. Gadgil argued for a clear statement of priorities; and the related question of the policies to implement the priorities. It is obvious that there can be no plan or even policy without explicit prioritization and an equally articulated policy framework. But this point needed to be made forcefully then as now. Politicians do not like priorities. They want to please everyone. And when you have a Prime Minister of boundless energy, enthusiasm, catholicity of interests and a propensity to fall in love with everything old and new, familiar or esoteric, it seemed almost vulgar to speak of prioritizing or choosing. Gadgil had a point which was noted but not taken to heart.

C.N. Vakil and P.R. Brahmanand argued—rightly—that the only way to increase investment without inflation was to make sure that there was sufficient supply of mass consumer goods. That meant prioritizing investment in consumer goods industries. This too was not dismissed in theory. The significance of the point was minimized, however, by arguing that mass consumer goods may not need much investment if we relied more on cottage, village or small-scale industry. Shades of Gandhi were mixed with Nandaji's[5] concern for employment and a wishful brew was concocted. Doubts were raised whether efficient labour-intensive techniques existed in many lines. Amartya Sen drew attention to labour-intensive techniques often being inferior rather than alternate in the sense that they might be capital-intensive and/or raw-material-intensive as well. The Economic Division study of Ambar Charkha done by Honavar had come to a similar conclusion.[6] But such qualms could be silenced by an appeal to subsidies or preference and protection—on the ground that employment generation in a labour-surplus economy could justify some subsidy for the employment of labour. Even before Mahalanobis appeared on the scene, the ground was being prepared at least for substantial investment in steel and fertilizers and for comparative neglect of organised consumer goods industry in favour of the small or village or cottage industries.

A frontal objection to the current consensus came only from B.R. Shenoy. For him, a bolder plan meant larger budget deficits and inflation and he would have none of it. I do not remember his taking the ultra-Hayekian line that all government investment expenditure was sinful. His was not a crusade for the private sector as much as it was for fiscal virginity. One wishes he was more forthright on the former and less so on the latter. He often misread statistics due to his obsession with his thesis and was much too abrasive for the times. The result was that he was heard, not listened to, and not even respected as Gadgil or Vakil and Brahmanand were, despite being overlooked.

To the best of my recollection, the question of an appropriate policy framework for the plan was never fully grappled with. To grasp that nettle properly, one has to start with a certain view of how the economy functions: who the main economic agents are and how to induce, compel or subdue and subvert them to suit plan priorities. That kind of discussion would have led to an examination of the appropriate spheres of activity of the public and the private sector and the ability of the former to influence the latter. The question of their relative competence or of the practicality or wisdom of certain kinds of state action were also not debated. In other words, neither alternatives nor implementability were given much thought. In part, this was the result of the belief in the wisdom and supreme ability of the Government. In part the Plan essentially was a statement of the intentions for public expenditure so that implementation was also seen essentially through the implementation of annual budgets. The rest of the paraphernalia of targets in the plan was either indicative or rhetorical. But even though the targets were indicative of what the private sector (together with the public sector) might achieve, they soon led to policy implications. If the private sector has to produce so much coal, that much capacity must be licensed and no more; if that

much capacity is to be created, the financial institutions must make loans in the appropriate amount to all those who were given licences. Why no more capacity should be licensed was a question not asked or answered; but the answer perhaps was in the notion that capital or savings are scarce and should not be wasted in excess capacity. How the required capacity was to be distributed among different claimants was also answered without reference to the market. Considerations of regional balance, ministerial preferences and party calculations if not pure bribes surely entered the picture. And no one asked why industrial capacity had to be licensed rather than induced by incentives and disincentives—not that these were excluded either. How industrial licensing came about and became a ubiquitous feature is an intriguing chapter in Indian economic policy. I suspect war-time experience, bureaucratic habits and regional pulls in a federal democratic structure must all have played a part. The Industrial Policy Resolutions of 1948 and 1956 are explicit statements; we did not simply stumble into this mess. But they are all rather porous or open-ended policy statements capable of admitting large areas of discretion. Over time, the discretion gravitated towards graft and ministerial or regional push and pull.

For the public sector, once the targets were set and expenditure provisions made, the task of implementation was basically one of project selection and preparation.[7] While much lip service was paid to both and to accounting price models and the like, projects were selected on traditional lines of internal rates of financial return much as in a private enterprise. But there was at least some attempt made in the early years to set up a Project Evaluation Unit in the Planning Commission. This unit did very useful work in introducing some discipline and rationality in project selection and formulation. But over time, the exigencies of foreign aid availability introduced distortions; and much later, all pretence of rationality was given up in favour of ministerial tug-of-war and discretion ending up in the prime ministerial monopoly of final decisions on major projects. The seeds of corruption were thus sown in the downgrading of the project evaluation process.

Thinking on the Second Plan in Delhi had advanced a great deal when Mahalanobis entered the fray with the blessings of both Nehru and Deshmukh.* But he had other credentials too. He was a man of great charm and formidable intelligence. He commanded respect in academia all over the world and was able to invite to the Indian Statistical Institute in Calcutta economists and statisticians of world renown for advice on the Plan. To name just a few, Ragnar Frisch, Tinbergen, Myrdal, Galbraith, Richard Goodwin, Oscar Lange and Charles Bettleheim spent weeks in Calcutta during 1955–6. Most, but by no means all, had leftist leanings. Indeed, some Russian and Chinese scholars were also there, the Chinese more to learn about sampling techniques than to advise, but they too had an input in terms of the thinking on their First Five Year Plan which was not very different from that in our Second Plan.

The presence of so many leftist advisers made the Americans urge that the Ministry of Finance allow some American advisers to balance the forces, so to speak. We thought we had the Americans hoist by their own petard when we agreed, with the proviso that there should be two advisers: one a distinguished academic and another with influence in Washington such as a member of the President's Council of Economic Advisers. We knew in Delhi, if not in Calcutta, that the Americans too had to be kept on our side. But the Americans had the last word: they sent Milton Friedman (an undoubtedly distinguished academic whose opposition to planning and government intervention in matters economic was total) and Neil Jacoby who was the former Chairman of the Council of Economic Advisers under Eisenhower. Neil's opposition to planning and governmental involvement can only be described as totalitarian, that is, extreme, ideological and emanating from the guts rather than from reason. Soon Friedman was so embarrassed by Jacoby that he requested they should be separated. This was easy to do as Neil and his wife were happy to be sent off on their own on a Bharat Darshan.

*New York, 24 December 1999.

Friedman tried educating Indian politicians and bureaucrats about the virtues of free and private enterprise, but soon gave up as he was intelligent enough to see that his arguments fell on deaf ears.[8] He asked me to arrange no more meetings but suggest something else he might usefully do. He jumped at my suggestion that he could sit down with our young researchers, see what they were doing, suggest improvements and further reading and generally improve their economic skills. He could not have been more hardworking and inspiring. Unfortunately, his visit was cut short for personal reasons.

I came to like and respect Friedman immensely; and although his views were then not fashionable in India or even in the US, the sheer brilliance of his intellect, skill in debate, historical knowledge and the cut and thrust of his arguments delivered fast and with good humour were truely arresting. Over many dinners and teas we were treated to how the principles of freedom could be applied to every sphere—not just economics, but education, social reform and the like. He was not without compassion or what we might now call an appreciation of government action to promote greater equality of opportunity for all. He favoured a negative income tax to give the poor additional incomes which they could spend as they like rather than specific subsidies or public provision. In higher education, he favoured a system of vouchers for all who had merit long before such ideas became familiar in the eighties. That there could be a case for the government financing something did not mean that government should actually provide that service. We were taught that lesson in the fifties, but forgot it and had to learn it again in the eighties.

A few years later, when I visited him in Chicago, he insisted on driving me around the area where the black population of Chicago was confined. He kept pointing out garishly painted houses, many of them with second-hand Cadillacs standing in front of them. He asked me what this told me; I was wondering if he was implying some slur on black tastes, which was unlike him. He offered the explanation: the black people have very little choice in life and little scope for showing that they had done better than

others by their efforts. We do not allow them to stay in clean suburbs in decent houses. We do not allow them to send their children to good schools. What have they left but to proclaim their difference or success by buying a Cadillac or painting their houses bright?

There is a moral sense to the competitive or free or capitalist economic system for it allows greater expression to individual freedom—as long as something is done to achieve greater economic opportunity for all.

It was during the autumn of 1955 that I was nominated as a kind of liaison officer serving as a link between the Ministry of Finance (and the Planning Commission) in Delhi and the Indian Statistical Institute (ISI) in Calcutta. I am sure my young age, which Mahalanobis must have thought left me relatively free of preoccupations or prejudice, was a factor. On the other side, Anjaria had implicit faith in me. I mention this as there was considerable resistance in Delhi to the intervention of Mahalanobis which prompted the idea of a liaison officer in the first place.

The few months I spent shuttling between Delhi and Calcutta were among the most rewarding in my life from many points of view.[9] The sheer intellectual and social excitement of rubbing shoulders with so many extraordinary individuals and the exposure to different ways of looking at things were rare treats. Mahalanobis and his wife could not have been more kind and hospitable. The ISI campus reminded one of ancient *gurukuls* set in sylvan surroundings. And there were constant arguments and discussions and lectures.

Apart from Mahalanobis and his colleagues at the ISI, I met and had varying degrees of interaction with a number of visiting scholars. Ragnar Frisch was rather frail and his wife allowed me no more than a brief *darshan* of him; and I cannot remember what exactly his special contribution to the debate was. Oscar Lange was equally non-communicative, but his exquisite and sociable

young wife more than made up for it. I had the distinct feeling that they were on the way to being disenchanted with Polish communism. Charles Bettleheim was a bit opaque like most Marxists. But the rest—Galbraith, Myrdal and Goodwin—spoke in familiar language and they and their spouses were very good company. Among all these distinguished visitors, I worked most closely with Goodwin and my association with him continued into the future. I am not sure if I met Tinbergen then—I did meet him later.

What came out of all these confabulations was a draft plan frame of the Second Plan which–in its first draft—I wrote out during my last visit to the ISI in Calcutta.* It was a kind of marriage between the work done in Delhi and that done in Calcutta. In the Planning Commission—with the help of the Ministry of Finance—projections were made of growth of national income (I believe at the rate of 5 per cent per annum) and savings and a rough picture of public financial resources available for investment. There was already some picture emerging of total financial requirements, and, therefore, of additional resource mobilization required. I am not aware of any detailed balance of payments forecasts. My memory is that there was some cursory discussion of a foreign exchange gap and the need for further claims on sterling balances and for external capital. At ISI, some physical targets of important items like foodgrains or steel or fertilizers were worked out on the basis of the assumed growth in incomes and savings and the first stab at input-output tables. There was, of course, no detailed work on the projects that would provide the required outputs or detailed investment allocations. That was to emerge later. The 'marriage' of physical and financial planning at that stage of a plan-frame was more notional than real, more postulated than proven or worked out.

Mahalanobis and I travelled to Delhi by train with several others from ISI, and the Professor read my draft—which had some of the economist's trappings about objectives and priorities—on

*New York, 27 December 1999.

that train journey. He was encouraging, but said that he preferred to present the frame in a different format and that the two of us should work on it together in Delhi. This we did in Delhi at his residence for the next few days. In the meanwhile, Anjaria worked on my draft. What emerged were two documents: the economists' Plan Frame and the Professor's. They were identical in every point of substance—of which there was not much really—and differed only in style. The Panel of Economists and the Commission endorsed them both as the basis for more detailed preparation.

It was about this time that Mahalanobis began to talk of his model which, in essence, emphasised that what we needed was not just more investment but more investment in investment goods industries as well—not just basic industries, but 'capital-goods to produce capital-goods'. Much has been said and written about this model—including by myself.[10] It was well known that it was a closed-economy model. But so were most other models of development then. This did not mean that the possibility of taking advantage of international division of labour was unknown or underestimated. It was not estimated at all. We suffered rather from export amnesia than from export pessimism.[11] What was underestimated was the difficulty in establishing an efficient capital goods industry, even steel and fertilizers, let alone equipment for steel plants and power plants. And the difficulty was compounded by the ideological decision to do everything in the public sector which had absolutely no experience in the field. But those were days of high nationalist aspirations and supreme confidence.

That a strategy to 'produce machines to produce machines' would increase investment requirements and might create a shortage of consumer goods was also known. But again, one was confident about mobilizing more resources and somehow allowed oneself to believe that less capital-intensive methods of producing mass consumer goods could be devised. There was little understanding then of a possible balance of payments constraint: the experience of the First Plan and the availability of sterling balances had made us sanguine.

What is not always realized or emphasized is that the Mahalanobis model or plan was never seriously or consistently

implemented in India—although echoes of it persisted for many years and some machine-building capacity was built in later Plan periods. Before any serious proposals to establish machine-building capacity could be considered and implemented—and indeed even before the Second Plan was finalized—we ran into serious balance of payments difficulties. By the middle of 1956 when T.T.K. arrived in the North Block, we were engulfed in a foreign exchange crisis which soon led to a hectic search for foreign aid and credits. From then on, it was the availability of this aid or those credits that set the pace of what projects were taken up, and with what kind of equipment. The Cold War gave us some leverage to exercise some choice of our own; and Mahalanobis's ideas did cast a shadow on the Third Plan. But the Second Plan—if it is seen as a Mahalanobis Plan—was still-born. In fact, what remained of planning after 1961—despite the succession of Five Year Plans—was little more than budgeting for Central and State expenditures while taking such advantage as one could of foreign benefactors. And considering our own inexperience, particularly in the public sector, in running complex industrial enterprises and the inevitable inefficiency of equipment, supplied under tied aid and Soviet credits, it is doubtful if we derived any advantage from much of the aid. The inefficiency was compounded by overstaffing for political reasons; and the financial costs were greatly increased by erecting on 'green fields' all the paraphernalia of major townships in addition to the plants and the roads and power supply. Some credits, particularly from the World Bank, were untied and given after much scrutiny and with large technical inputs. They did do some good. But the same cannot be said of bilateral aid. Of all inefficiencies, the most damaging is that of the superstructure of equipment and capital-goods industries, and generation of power and economic infrastructure in general: such inefficiency percolates to all sectors of the economy. It is like poisoning a river at its very source. It is little wonder that we had such an adverse capital–output ratio. We concentrated where we had little comparative advantage; and we compounded this by accepting doubtful gifts from actual and potential competitors—and by making a fetish of public ownership.

The Foreign Exchange Crisis of 1956

What exactly led to the foreign exchange crisis of 1956? The conventional wisdom is that it is the bold and ambitious Second Five Year Plan that was the culprit. This is only partly correct. The Plan period began in April 1956; and the final Plan document came much later. True, some of the ideas and projects in the Plan had begun to be implemented when the Plan period began—particularly in the steel and fertilizer sectors. But Deshmukh's last Budget of 1956 hardly set a new trend. If there was any new trend it was in the Export-Import policy of April 1956 which entailed considerable liberalization of imports to speed up growth. I cannot recall who initiated this or what its rationale was. I was not involved in day-to-day economic policy then, being catapulted instead into the stratosphere of planning strategies. But I think the subsequent economic history of India owes much to that import liberalization; and I hope somebody someday will probe further into that chapter.[12]

The Finance Ministry's response to the foreign exchange crisis was prompt and wide-ranging. B.K. Nehru who had recently returned from Washington to take charge as Joint Secretary in charge of External Finance set about preparing a foreign exchange budget which would serve as the basis for determining how much import we could afford and, therefore, permit the Commerce Ministry to license. He was ably assisted in this by his deputy, Ezra Kolet. It is noteworthy that foreign exchange budgeting began and was elaborated not in the Economic Division but in the regular administrative division of the Ministry manned by civil servants rather than economists. Later, we and the Reserve Bank provided inputs for this regular six-monthly exercise which assumed much greater importance when the era of foreign credits and aid began and we had to maintain a careful watch over our credit receipts and debt payments. If we regulated wisely how much we could borrow and on what terms each year and made sure that we maintained our credit-worthiness by honouring all our obligations on the appointed day, the credit for it must go largely to this discipline of foreign

exchange budgeting started by B.K. Nehru. To this day, we have never delayed in meeting our debt obligation, let alone reneged on them or repudiated them. The age-old Indian custom of sons paying the debts of fathers and grandfathers has been honoured also by the Indian nation for more than 50 years now.

B.K. Nehru had liked some of the briefs I had prepared for our UN delegations—and had taken the trouble to tell me so. Thus began a lifelong relationship during which I have received unfailing support, encouragement, guidance and affection from this most gifted and noble civil servant. In a way, if Anjaria led me into economic advice, B.K. Nehru propelled me into economic diplomacy. H.M. Patel too had taken upon himself to train me in economic administration and T.T.K. made no secret of the fact that he was preparing me for higher responsibilities. A Coordination Committee consisting of secretaries of relevant ministries was formed under the chairmanship of H.M. Patel and he appointed me as its secretary. My job was to keep minutes and to pursue the implementation of decisions taken. It was superb training. It brought me face to face with actual problems of day-to-day economic life and the bureaucratic, legal and political hurdles in actual implementation. I wish I had access to the minutes of this committee. All I can do now is to recall a few incidents in which I was involved at that time as the secretary of that committee and thereafter. The committee was rather short-lived as it was overshadowed by the Mundra crisis (discussed later). But the tradition of inter-ministerial consultation and my involvement in it continued.

One of the early responses to the foreign exchange crisis was to reduce the foreign exchange backing for Indian currency. We could not draw down the sterling balances to the extent it seemed necessary in view of the proportional reserve requirements in operation then and the government's need to borrow from the RBI. Having been brought up on Keynes and his argument about the stupidity of such requirements,[13] I sent a note to B.K. Nehru recommending a change to a requirement in absolute terms. This was what the doctors ordered and what the patient wanted—and the law was changed.

Alas, we were about to run through the extra leverage also very quickly and Nehru proposed a reduction in the absolute amount. This time, I opposed the change to the surprise of everyone. Nehru could not understand why I had forgotten my own reasoning. The matter went to T.T.K. for decision. T.T.K. called a meeting of all his advisers, including L.K. Jha from Commerce, and of course Patel, Nehru, Anjaria and Bhattacharya. I was asked the reason for my stand—which was based not on reason but on gut reaction. On the spur of the moment, I said: 'Reserves are for covering mistakes. Your generation got Rs. 1500 crores to cover up your mistakes. I want at least Rs. 500 crores to cover the mistakes of my generation.' T.T.K. was angry and said they were leaving enough for my generation—three steel plants, three fertilizer plants and so on. Was that not enough? But he ended the meeting by saying: 'Very well, I.G. will have his 500 crores.' There the matter rested. No one talked of changing the reserve requirements after that.

It is pertinent to recall that in 1999, there were many voices raised in favour of going back to proportional reserve requirements and even further to a Currency Board system linked to the gold or the foreign exchange standard: not a single Indian rupee can enter circulation without an increase of one rupee in foreign exchange reserves and, horror of horrors, if you lose a rupee in foreign exchange, you have to reduce the currency in circulation by that much! History does repeat itself.

It was around then that we decided to withdraw Indian rupees from circulation in the Gulf countries, Kuwait and parts of Iraq and elsewhere in the Middle East. India was the jewel in the British crown and the hub of Britain's naval and commercial empire; and the Indian rupee circulated widely in the Middle East as a medium of exchange and store of value—a reserve currency, no less. But this prestige meant that we had to convert at least into sterling all the rupees tendered to us from that region. That made smuggling of gold into India easy to finance. One only had to take the rupee proceeds out of India and return them to India for conversion into sterling to buy another round of gold for smuggling. It was thought this drain on our reserves could be stopped once

and for all by converting into sterling all the rupees circulating abroad. Thereafter, the rupee would be inconvertible.

The shades of British Empire and the dreams of rupee as a reserve currency have vanished into thin air, but not smuggling of gold into India. Only the transaction costs of smuggling have increased; but there is hardly any reduction in the amount smuggled. Other means of financing like overinvoicing of imports and underinvoicing of exports were readily available. Given the subsequent history of Middle Eastern prosperity, the inevitable could not have been avoided for ever. But surely, nothing would have been lost by waiting till the initiative came from others. Again, one of those imponderable counterfactuals. Today, it is not India but the US (and to some extent Pakistan) which has inherited the economic and military clout once enjoyed by the British in the Middle East.

The foreign exchange crisis also led to the first foray in obtaining foreign credits. Since the sterling balances were declining, it was felt that we should ask the Bank of England for an overdraft—I believe of £200 million. We thought it was our right to obtain a modest overdraft from a Bank with which we had kept large deposits for many years, at low rates of interest and suffering depreciation to boot. H.M. Patel and I were sent to London—my first exposure to what was to be a long-term saga. H.M. was confident that he would have his way. He knew Sir Leslie Rowan in the Treasury and called on him before going to the Bank of England. We were told politely but firmly that the Bank of England never gave overdrafts and that they would not like to set a new precedent. This was confirmed by Maurice Parsons in the Bank, and our mission ended in two days. So much for the solace of sterling balances and the Englishman's sense of fair play. The alternative of a British government loan was neither asked nor offered.

One memory of that visit was that at H.M. Patel's instance, I introduced Manmohan Singh, who was then at Cambridge, and Ratan Bhatia, who was at Oxford, to him. H.M. was keen on recruiting bright economists and both were offered jobs on the spot. Bhatia actually joined our Division for a while on his return from Oxford. Manmohan decided to return to his University in Punjab.

It must be in the autumn of 1956 that I went to New Zealand to attend the annual meeting of the Colombo Plan.* It was just after the Suez War, and our support for Egypt had not made us popular in the UK or indeed in New Zealand. The Colombo Plan meetings then were leisurely affairs held in three stages. The first of about a week was attended by junior experts who prepared draft reports on each recipient country on the basis of materials supplied; the second of about three or four days was where senior officers finalised the report for consideration by the ministers; and in the third of a couple of days, ministers adopted that report and made some announcement of intentions. My seniors failed to arrive at the last moment—and I spent a pleasant three weeks in New Zealand, as an expert-cum-senior civil servant-cum Minister!

I was to learn within a day or two of my arrival in Wellington—from a Canadian delegate called Rodney Gray who became famous later on as a salesman of Canadian wheat to China—that the British were on the war path against India. They were peeved by Suez; and by our flirting with a bold plan of industrialization and with socialism and by our acceptance of Soviet aid. Our example was being followed—and Nepal and Cambodia too had got some Communist aid. According to Rumbold of the British delegation, this had to be stopped and India must be taught a lesson. He was trying to work on others to support this line in the meetings of the donors. The Americans were sympathetic to this line of thought, but the Canadians, Australians and New Zealanders were uneasy about the tension (although New Zealand, for example, did not agree with our stand on Suez). This was the first important international meeting in New Zealand, and they did not want any unpleasantness.

I had to think fast as to what to do; and I decided to concentrate on the leader of the US official team. At a reception, I cornered him and asked him if he knew that India had become independent in 1947 and that since then anyone who had anything to

*New York, 28 December 1999.

discuss about India had to do so with India and not with Britain. He knew what I meant and was a bit surprised. I gave the same message to others and showed my willingness to discuss anything.

The strategy worked—and I had, of course, talked to the Nepalese, Cambodians and the Sri Lankans for support. At the official meeting, all references to our plan and to Soviet aid were retained as statements of facts—not necessarily of approval as the Colombo Plan was not called upon to approve our plan. Technical assistance under the Colombo plan was of marginal importance to the implementation of our plan.

Strangely, all Colombo Plan documents till then referred to the release of sterling balances by Britain of, I think, £30 million per year as British 'aid' to India and Britain as the largest aid donor to India. I decided to be aggressive much to Rumbold's discomfiture: I argued that allowing our own money to be used could not be termed aid—it was only partial repayment of a debt due. The point was so obvious that all reference to British aid was dropped. But it is interesting to note that in the vocabulary of aid, it is the giver who takes all: suppliers' credits at high rates of interest, tied aid repayable in foreign exchange and even meeting one's debt obligations and perhaps even reducing restrictions against one's exports can all be called 'aid' or 'assistance' or 'accommodation'.

The visit to New Zealand also witnessed the first aid exclusively negotiated by me—and the best aid that India has ever obtained at that! I had come to know well the New Zealand Finance Secretary, Moriarty,[14] during the meetings and he told me that New Zealand would like to be a donor in the Colombo Plan and would like to begin with India. They could only approve a small sum of about £1 million, but would like to give it with as little fuss and bureaucratic rigmarole as possible. He wanted some suggestions. Ultimately, a gift of £1 million was agreed upon, to be given in cash to the Government of India with the only stipulation that some mutually agreed project would bear the inscription proclaiming the aid from New Zealand. The project chosen was the All India Medical Institute in Delhi. This record of a cash gift and no questions asked or any real favour expected or granted, remains

unbeaten for India till today. Even the New Zealanders, to the best of my knowledge, unfortunately did not find this experience habit forming!

*T.T.K.: The Expenditure Tax**

T.T.K. came to the Ministry in the summer of 1956 all pepped up to make a mark on India's financial history. That was his nature: vanity with a touch of childishness and exceptional ability combined with a mercurial nature which knew only extremes of likes and dislikes. For some reason, Anjaria and myself were high on the 'likes' list from the outset. We were, as mentioned, moved near him in North Block. Since the regular budget was months away, T.T.K. wanted to do something as an interim measure. If I remember right, Anjaria suggested some tax measure relating to textiles which T.T.K. initially opposed. He, however, introduced the measure in Parliament; and when it was well received, took the credit for it, even telling Anjaria that he (Anjaria) was wrong in opposing it—just the opposite of what had actually happened.

T.T.K. was happy to invite Kaldor to advise on tax matters; and the few weeks that the Kaldors spent in India were very rewarding for me. K.N. Raj and I became very friendly with the family (Nicky and Clarisse and their two daughters, Catherine and Frances) and visited many places together including Agra and Khajuraho. Kaldor had been my teacher and examiner; and he and his family have showed great affection for me over the years. I too have learnt much from Nicky during our several encounters—which included in later years membership of several expert groups set up by UNCTAD, including the one before the first UNCTAD conference and two or three under the leadership of Sidney Dell on International Monetary Reform.

Kaldor's visit to India in 1956 is known most for his recommendation of an Expenditure Tax. His views in favour of the tax were already formulated and about to be published in book form (he gave me a proof copy). But he needed to understand the

*31 December 1999.

Indian tax system and tax administration to devise an operational tax proposal. He applied himself to this task very diligently and was ably assisted in this, I believe, by Iqbal Gulati and Amaresh Bagchi. What emerged was the idea of a comprehensive tax system with a low income tax combined with an expenditure tax, a wealth tax and a gift tax. Given a combined return of income, gifts and changes in wealth, expenditure would be derived without much difficulty; no direct returns of expenditure would be called for. If I remember right, while the income tax rates were to be low, the expenditure tax proposed was high.

T.T.K. was bent upon implementing this. Introducing a new tax for the first time could be his passport to a place in history. I was generally in favour of the Expenditure Tax—as I still am—but had no idea of tax administration. Anjaria was willing, I think, to give it a try. The mainstream officers, including B.K. Nehru, were opposed to it. The fear was a possible loss of revenue in trying the unknown and drastically lowering the income-tax. The compromise adopted in the Budget of 1957 was the worst possible—a high expenditure tax superimposed on a high income tax combined with a new wealth-tax and a gift tax. The total incidence was crushing, exceeding 100% in some cases. The Expenditure Tax proved short-lived. (It must have been removed in 1959). But its short-term consequences were grave.

The Mundra Affair

The immediate effect of the 1957 Budget[15] was a crisis of business confidence and a sharp downturn in share prices. T.T.K. knew enough of the functioning of markets to know that it was imperative to revive business sentiment. He turned to the idea that the newly formed nationalized Life Insurance Corporation (LIC) could buy up shares when prices were tumbling. This would stabilize the market and could also be profitable for the LIC.[16] There was some merit in this line of reasoning. But something went awry.

Either because of the desire to avoid criticism that a public sector financial institution was being used for purposes not central to its business or simply with a view to take the market by surprise,

it was felt that LIC purchases of shares should be made as quietly as possible. Someone—perhaps a broker or a middleman—suggested the purchase of shares in some Mundra companies as Mundra was in financial trouble and was anxious to keep his distress sale as quiet as possible. Instead of buying quietly in the open market, a deal was struck with Mundra for purchase of a large amount of his shares in the hope that this would change market sentiment and LIC would have made a good purchase.

Inevitably, there was an uproar in the Parliament and the country and there were accusations of a political deal or worse. Whoever took the initiative in suggesting this course of action, there could be no question that it could not have been taken and implemented without T.T.K.'s approval: he was always a hands-on minister and not just a political leader content to let his trusted advisers act on their own. It was also in keeping with the highest traditions of parliamentary democracy that the minister should take responsibility and resign. But T.T.K. had invested too much personal pride and ambition in the office of the Finance Minister and was unwilling to let it go. To the utter shame of the Prime Minister, it must be said that he too did nothing to ease out one of his favourite ministers.

There were rumours galore involving all and sundry in some improper action or the other. The general public is only too willing to believe the worst of those in authority. H.M. Patel, the Finance Secretary, and G. Kamat, the Chairman of the LIC, were all but condemned by official unwillingness to defend them. Justice Chagla was asked to hold an open inquiry which he did with flair and with his heart set on popularity. That he had political ambitions became clear soon when he accepted an ambassadorial and subsequently ministerial position. His Report, without being conclusive, cast doubts on the propriety—if not probity—of the action of T.T.K., H.M. Patel and Kamat.

I remember that there was a meeting of the Panel of Economists in the Planning Commission during the Chagla hearings and the

general feeling among all economists present was that T.T.K.* had behaved disgracefully: he did not defend Patel or Kamat and made instead equivocal statements which could be interpreted as implicating the two. He assumed no responsibility for himself. It was also felt that H.V.R. Iengar, then Governor of RBI and the Expenditure Secretary, P.C. Bhattacharya whom T.T.K. trusted greatly and apparently consulted regarding the Mundra transaction, were also economical with truth: they did not defend their colleagues as that would have displeased and even compromised the minister.

The day after T.T.K.'s evidence, some of us were lunching in my room at the entrance of the North Block and were heatedly condemning T.T.K.'s action. In walked T.T.K. himself, as was his habit; whether he heard us or not, I cannot tell. But immediately, he proceeded to tell us how suffocating and unsettling the atmosphere during evidence was, how glaring the lights were and how large the crowds. In that atmosphere, T.T.K. said, one could not be sure what one was saying and how one's words might be interpreted. He may even have praised Patel and Kamat.

I am not sure about the exact sequence of events. But Kamat and Patel went on leave and their role was given for inquiry to a one-man commission composed of Justice Vivian Bose. Eventually, they were fully exonerated. Patel refused to return to his civil service career and carved out for himself a totally new and far more rewarding career as educationist, social reformer and creator of institutions in a number of fields, including health care and education through the English medium in Gujarat and translation of classics into Gujarati. He even excelled in politics and became the Finance Minister in Morarji's Government in 1977. If ever there was a case of vindication with a vengeance, it was that of H.M. Patel. I do not know what Kamat did after taking voluntary early retirement. But I have no doubt that this modest and gentlemanly ICS officer was honest to the core and unlike some of his other colleagues, loyal to H.M. Patel even at the risk of jeopardizing his

*New York, 4 January 2000.

own position. Indeed, he remained loyal even to T.T.K. by owning responsibility as Chairman of LIC.

During the Vivian Bose inquiry, H.M. Patel asked me if I could help him with his defence by writing some notes on the economics of the whole affair; and I consider it one of the most honourable things that I have done that I took leave for one week, stayed with Gorwala[17] in Bombay and did what I could. D.R. Gadgil too was helping H.M. When H.M. became Finance Minister in 1977 and I called on him, I could not resist saying: 'It is so good to see you in this particular chair.' He knew what I meant, but quietly changed the subject. He was not interested in dwelling on the past; and I have never heard anyone say that he or she had heard H.M. speak on this matter.

Over the years, stories have circulated about one particular individual having suggested the Mundra deal. Knowledgeable persons whom I admire and respect had given—in private conversation—credence to this rumour which is certainly plausible. But after some thought, I have decided not to give further credence to the story. After all, I have no way of knowing the facts; and the person could have acted in good faith. Without trust, life is impossible despite the fact that trust may at times be misplaced.

For T.T.K., the reprieve proved short-lived. Since H.M. and Kamat were exonerated, who was responsible? At least, by parliamentary tradition, T.T.K. was. This was loudly proclaimed in Parliament, and ultimately Panditji not only had to ask his favourite minister to go, but had to invite someone not his favourite but known for his probity to take T.T.K.'s place—Morarji Desai. That this could not have been palatable to Panditji but was done to allay public opinion became clear very soon when Panditji took the first opportunity to shunt Morarji on to the Administrative Reforms Commission. He had already brought T.T.K. back as Minister of Economic and Defence Coordination. But this is to anticipate.

T.T.K. : Beyond Kaldor and Mundra

T.T.K.'s first term as Finance Minister should not be judged simply by the bravado of the Expenditure Tax or the fiasco of the Mundra affair. He brought much vigour, debate and discussion

into the working of the Ministry. He was keen on training young economists and officers; if he had favourites, he chose them irrespective of caste or tongue and took them in hand, looked after them and saw to it that they had a wide-ranging exposure. He had favourites—and devoted followers—among senior officers too, and he welded his team, drawn from several ministries, well together. In this sense, he was truly 'the Economic Minister'. It was also during this period—1956 to 1958—that we began our long journey on the road to foreign aid, comprehensive import and foreign exchange control, rigorous industrial licensing, socialism, or the attempt by the public sector to occupy the commanding heights of the economy. Not all this was T.T.K.'s doing; and, indeed, I cannot believe that he had much sympathy with the flirtations with socialism or the Soviet Union. But his admiration for Panditji was so total and even unthinking—strange for a man like him—that he went along. I am convinced this was not opportunism. It was hero-worship—again, evidence of his strong likes.

By the time T.T.K. arrived in the Ministry in 1956, the foreign exchange situation had already become difficult; I have already recorded some of the initiatives taken to stem the tide. There were limits to the withdrawal from sterling balances as well as to what we could borrow from the IMF. The World Bank too had measured our creditworthiness strictly and concluded that we could not service World Bank loans of more than $50 million per year. Aid, as we know it, was not yet on the cards. At the same time, imports related to on-going projects and essential needs could not be curtailed beyond a point. Attention thus turned increasingly to supplier's credits, and especially to Soviet type credits repayable in rupees. The Rourkela steel plant was undertaken on the basis of suppliers' credits of two or three years' duration. This was soon found to be onerous and we had to renegotiate the terms of the credit by spreading out repayments. I spent nearly three weeks in Bonn in this connection with an officer from the Steel Ministry. We were to negotiate under the guidance of T. Swaminathan who, as Economic Minister in the UK, was given charge of economic negotiations in Western Europe. This was a rewarding experience for me. I came to have an idea about Germany and the German

miracle. The office buildings were the war-time barracks, and even the senior officers lived in such cramped quarters that they regretted they could not entertain us at home. To save resources for investment in industry, housing and offices had to take a back seat.

During a visit to the Demag works, we were also told how the steel and machine-building industry was rebuilt so rapidly after the war. All the plants had been turned into rubble by allied air strikes. But when the war ended, all the old workers—maimed, wounded or healthy—returned to the old factory site with their families. The owners too returned; and together, they made do with whatever was available. Children were also taught whatever the women could teach them. Everyone had a sparse ration. Soon, they were producing and selling some things and making money, which was not difficult in an economy of shortages. But it was agreed that all surplus would go into reinvestment—the owners would take the minimum for their daily needs as would the workers. With rapid reinvestment, the plants were rebuilt and even modernized and both owners and workers could resume their earlier living standards. Corporatism was the economic aspect of fascism—and in Germany and Japan, it survived the excesses of fascism in other spheres of life. The current wisdom is that such a system means imperfections in labour markets and should be replaced by unfettered competition. I am not sure if some assumption of common interests and willingness to cooperate for these common interests by workers and employers alike is not the kind of cement that is still necessary to hold societies together in good times and bad.

The Annual Meeting of the Bank and the Fund in Washington D.C. in 1957 gave us a good opportunity to plead for assistance to India in world forums. T.T.K. and his entourage (which included B.K. Nehru, L.K. Jha and myself among others) visited London and Canada on the way and Germany on the way back. (Some of us went to Italy too.) By then, I had become T.T.K.'s speech writer, and I worked hard at nights to turn out a speech or two for the next day.

The Commonwealth Finance Ministers' meeting in Mont Tremblant in Canada was historic in a sense: it marked the final burial of Imperial Preference.[18] Diefenbaker, the Canadian Prime Minister, felt that the idea of Imperial Preference could be revived as a counterweight to Britain's entry into the European Common Market. No one else agreed with him, and the idea of Imperial Preference died a natural death. In that environment, arrangements like the sterling area could also no longer be maintained. Thus ended the economic arm of the British Empire, along with its political and military might.

The speeches T.T.K. made in Washington and New York had a special purpose: they were designed to convince the Americans that we did believe in private enterprise and private property, that we were not communist stooges and that our socialism was of a special type. Much clever drafting went into this kind of 'neither this nor that' argumentation, and T.T.K. often tilted towards the 'private sector' angle in his verbal elaboration of the written text. This created much furore in Parliament: T.T.K. would send the written speech to newspapers in Delhi and Krishna Menon and his flag carriers would brief the journalists—with some salt and pepper added—on what T.T.K. had ad libbed orally. As long as John Foster Dulles was alive and Krishna Menon and he delighted in verbal duels, there was little scope for creating sympathy for India in the US. But in the later period of the Eisenhower administration, despite Menon, it was possible to get some hearing in Washington and New York. T.T.K. did see Eisenhower in Washington and was entertained at dinner by David Rockefeller in New York. On the way back, we stopped in Bonn and Erhard entertained us with a boat trip on the Rhine. The ground for aid to India was being laid—and B.K. Nehru and others laboured hard to prepare it. T.T.K. deserves much credit for appreciating that the goodwill of the US was important for India and cannot be taken for granted. It is also interesting to recall that one of T.T.K.'s advisers and facilitators during this trip was George Woods who used to advise us on investment then and who became President of the World Bank later after Black. In fact, to emphasize

the relationship, George Woods had actually come to the Idlewild airport when we first landed in New York on the way to Washington. I record this as it is not irrelevant in the context of our soured relationship with the Bank in the sixties in which George Woods and T.T.K. were to be the main protagonists.

On the domestic front, economic policy began to be crystallized around detailed industrial licensing, preferences for the small sector, rigid control over imports and foreign exchange, attempts to equalize access to important raw materials and industrial goods through freight equalization and the assertion of socialism: not as yet through nationalization of existing private trade, industry or financial institutions but through greater and greater reservation for the public sector. As a corollary, private foreign investment instead of being actively promoted and welcomed came to be grudgingly accepted in select cases after much delay and under several constraints. To explain all this in terms of personal predilection, for example, Pandit Nehru's fascination for socialism or the Soviet Union or the Fabians, is too simplistic and certainly only partly true. What was Nehru not fascinated by? The reasons were many. I suspect the divisive character of the Indian society, the need to preserve the Indian federation, the workings of a Parliamentary democracy where a hundred and even a thousand flowers have to be allowed to bloom, all led to a kind of ecclectic melange where every policy of special pleading found a place. Once introduced, each policy acquired its own momentum and vested interests and became difficult to limit, let alone reverse. If the private sector was controlled, so was it protected, assisted and coddled. There were also other influences: the overpowering sense of a scarcity complex generated by the foreign exchange crisis, the inability of the Indian private sector to handle very large projects and the fear of a resurgence of foreign domination through large-scale foreign investment.

I have already referred to industrial licensing. I presume it is the concern for employment and the anxiety about shortage of

savings that led to reservation for the small-scale and cottage sectors. The Gandhians too must be accommodated. At the other end, I do not think Indian industry was ready then to undertake large projects like steel plants or fertilizer plants. I do not remember great enthusiasm even among the Tatas for substantial expansion of their steel production. J.R.D.'s Air India was not nationalized. He was too happy to hand it over to the Government, as he was to hand over the Tata Institute of Fundamental Research and the Tata Cancer Hospital. Sir Biren Mukherjee, despite all the support of the World Bank, was not able to manage his modest steel plant. Let us not forget that even the great and the good in Indian private industry had little access to world capital markets then. Even Europe was enmeshed in exchange controls. It was the consumer goods industries in the organized private sector which really suffered because of the reservations for the small sector and the effective elimination of competition by licensing only a limited capacity to each producer in order to spread the gravy around.

The suspicion of private foreign enterprise was real and was reinforced by the belief that repatriation of high profits might strain foreign exchange reserves. Hence all the restrictions on the expansion of foreign enterprises already in India and stipulations such as export performance. At the same time, it would be wrong to assume that many new foreign ventures were knocking at the door and were turned away. The most notable exception to this was the proposal of the US steel industry to set up a private steel plant—the so-called Bechtel plant which was not granted a licence after protracted negotiations and which did much to assure the antipathy of the US steel industry towards India. This was a ghost which India had to fight hard to lay to rest over a number of years.

I still do not know for sure who thought up the idea of freight equalization. I suspect it was T.T.K. who did not want Tamil Nadu to be at disadvantage as it had to import coal and iron ore or crude steel from long distances. In a federation, such devices had an obvious appeal. If huge national resources are to be deployed to develop the coal and iron ore resources of Madhya Pradesh or Bihar or West Bengal, should not the benefits be shared by other states such as Tamil Nadu, the Punjab, Gujarat, and Maharashtra? This policy certainly helped the small and medium industries in the south, the Punjab and the west. But by the same token, as Ashok Mitra never tired of pointing out—and rightly—it denied West Bengal, Bihar and Madhya Pradesh the one natural advantage they had against their general lack of an industrial infrastructure. Later, similar arguments were to be applied to fertilizers, foodgrains and crude oil to the advantage and detriment of different states. To the best of my knowledge, no study exists of the costs and benefits of this policy which is a classic violation of the principles of free and unfettered competition. But it is not difficult to see how such a policy got adopted, continued and even flourished without much opposition or furore. Distribute the favours, ration the real or imagined scarcity because it may be a zero sum game after all. The result may be inefficiency and impoverishment. But there is a balance or equilibrium of sorts in equal satisfaction and dissatisfaction across the nation. No one thought that a different distribution of satisfaction and dissatisfaction in a more competitive environment might have led to more growth and less impoverishment.

How import restrictions came into being is not much of a mystery. They started during the war and were intensified after the 1956 foreign exchange crisis. But how do we explain DGTD[19] clearance under which nothing could be imported without proof that it cannot be or is not produced at home? How was a developmental agency for technical upgradation reduced to an agency for the absolute self-sufficiency syndrome? And worse, how was the amount that had to be imported to be divided among different importers? Similar questions can be raised about foreign exchange control. The scarcity complex, bureaucratic mentality, growth of vested interests and false notions of national pride and the consequent suspicion of foreigners, all played a part.

What is amazing is that all this happened in a country where there were strong protests raised against controls in the early years of Independence by no less a person than Gandhiji, supported by Patel, Rajendra Prasad and Rajaji. They firmly believed that

controls led to corruption and must be removed as soon as possible. They also believed in private property and limiting the role of the State as they saw the State as essentially an agency restricting individual freedom and responsibility. After all, Gandhiji wanted the Congress Party to dissolve, the big state to disappear and be replaced by small city states. But Gandhi, Prasad and Patel died early. And Rajaji was forsaken by his business friends who initially supported the Swatantra Party but soon abandoned it when they discovered that bribing politicians to get the licences they wanted was easier than acquiring political power with a view to changing economic policy towards greater freedom and competition. Those in business who now proclaim loudly the stupidity or cupidity of earlier political leaders should also examine the behaviour of the early business leaders. They wanted not competition and efficiency but to preserve and enlarge their own turf.

Somehow, the country became the antithesis of the consumer. In the quest for the country's good, the pride of place went to the government and to farmers, industrialists and organized labour. A whole new class of file pushers and rent seekers was created. The consumer was forgotten.

Endnotes

1. The early recruits to the Division included Ranganekar, Harbans Lal, S.S. Marathe, R.M. Honavar, A.K. Ghosh, Ashok Mitra, K.G. Vaidya, Barpujari, P. Dasappa and Manu Shroff.
2. Alas, this dinner also reminded me of the shape of things to come. I had no car and at the end of the dinner, I had to make small talk with Mrs Gandhi till the taxi arrived. Quite casually, I referred to newspaper reports about her accompanying the Prime Minister on a foreign trip. She literally shouted in anger that the newspapers were always after her, that she had never accompanied her father on any foreign trip except once when he was not well and so on. I did not know what had hit me—or her. But in retrospect, it is obvious that Mrs Gandhi was suspicious by nature and saw disapproval and even hostility where none existed. Those failings ultimately clouded her vision and actions, and also the reputation, which she undoubtedly deserved as a true patriot and a dedicated and talented leader. One dark spot on the full moon or on a lady's face might enhance the beauty. But a single dark spot on the leader can be the cause of his or her undoing.

3. In December 1954, Parliament passed a resolution accepting 'a socialistic pattern of society' as the objective of economic policy. The term 'socialistic'—Anjaria's contribution—speaks for itself. There were attempts also to explain rather apologetically that this resolution was not 'an attempt to copy any set pattern evolved elsewhere'. Cf. p. 12 of *India*, a publication of the Publications Division on the occasion of the 12th session of the ECAFE in Bangalore in January 1956.
4. The Parliamentary resolution on 'a socialistic pattern of society' was passed in December 1954; but it hardly had the ringing tones of a socialist manifesto.
5. Gulzarilal Nanda was the Deputy Chairman of the Planning Commission at the time and a labour leader in his earlier years.
6. R.M. Honavar, studied the economics of various Ambar Charkhas in actual production to determine whether they were labour intensive or capital intensive or both in coparison with textile mills.
7. Here too, there was much intellectual activity concerning how to go about it efficiently. Ian Little and Jim Mirlees—and at a later stage Amartya Sen, Partha Dasgupta and Steve Marglin—had attractive formulations of the right methodology for project selection.
8. He did submit a 'Memorandum to the Government of India 1955' which has recently been reproduced in *Friedman on India* published by the Centre for Civil Society, December 2000, New Delhi.
9. My wife to be was in Calcutta then.
10. 'The Strategy of Indian Planning' prepared in March 1963 and published in a volume in honour of Mahalanobis on his seventieth birthday entitled *Essays in Econometrics and Planning*, Calcutta, Pergamon Press, June 1964. Reprinted in my *Essays in Economic Policy and Economic Growth*, Macmillan, 1986.
11. It should also be emphasized that whether amnesia or pessimism, it was very short-lived. After the 1956 foreign exchange crisis, we indulged in export promotion and export subsidization as vigorously and indiscriminately as import substitution. We even pleaded—with some success—for preferences in developed markets for exports from developing countries. Cf. my article on 'Exports by Countries in Process of Industrialisation' prepared for the Chatham House conference at Bellagio in September 1963 and reproduced in the conference volume entitled *New Directions for World Trade*, Oxford University Press, 1964. The

same theme of special treatment of both exports from and imports into developing countries was repeated in several UNCTAD Conferences. Our original sin was failure to be selective by stages in both export promotion and import-substitution as Korea had done in imitation of Japan.

12. In his anniversary address in January 1958 to the National Institute of Sciences, Mahalanobis refers to 'the grave difficulties created by the shortage of foreign exchange' and adds: 'It is not surprising that mistakes have been made at the stage of transition from a small to a much bigger scale of planning economy. In a single year, 1956–7, our imports suddenly exceeded exports by Rs. 440 crores.'
13. Keynes compared this practice with a rule that at each taxi stand, at least one taxi must remain till another arrived. This would only immobilize some taxis and make matters worse. In his view, foreign exchange reserves should be limited to only such amounts as should not be touched except in an extreme emergency.
14. The Permanent Secretary in charge of finance in the New Zealand government at that time.
15. T.T.K.'s 1957 Budget speech is memorable in many ways. He wanted it to be, as he felt he was doing something truly path-breaking. He wanted me to draft a suitable peroration and I had to submit several drafts to him before he approved one with Churchillian overtones.
16. Life insurance business was nationalized under Deshmukh in 1952 and the LIC was formed as a public sector monopoly in this trade. I am not sure what prompted the nationalization. But it had in all probability practical rather than ideological justification such as avoidence of abuse of private savings.
17. A.D. Gorwala was a distinguished ICS officer and a friend of H.M. Patel.
18. The preferential treatment of each other in matters of trade in the membership of the British Empire began during the depression years of the early thirties and was a matter of considerable controversy within Europe and outside. After the war, with the growing interest in Europe and the US, Britain—unlike some of the Dominions—was no longer keen on these preferential arrangements.
19. Directorate General of Technical Development.

3

Washington D.C. 1958–61

*Vintage Nehru**

Morarji Desai came to the Ministry of Finance in the spring of 1958. By then, it was settled that Bibi (my wife, Alakananda Dasgupta) and I would be married in November 1958. The marriage could not be held earlier as both Bengal and Gujarat consider the four monsoon months (when gods sleep and humans work the hardest in the fields) unsuitable for frivolities like weddings. Whoever thinks that India is too diverse to be considered one nation should ponder over the similarities in wedding and other rituals throughout the land. With the impending change in my personal status, I thought it was time to make the professional change to teaching that I had always dreamt of. It would also suit my wife to be as she too wanted to teach. V.K.R.V. Rao offered me a chair at the Delhi School of Economics and I tendered my resignation from the Government job. Morarji sent for me, and asked me if I was sure I wanted to teach. I answered I was, and my resignation was accepted.

But events moved swiftly to change the course of my life. As soon as I informed Dr Rao that I was ready to join him, he gave me

*New York, 9 January 2000.

the shock of my life. He said he had thought over the matter and felt that I should join the newly set up Institute of Economic Growth, which was a research institute and not a teaching one. This was not what I wanted. I had neither appetite nor aptitude for research. It was teaching and the company of bright young people that I desired. It was at that stage that B.K. Nehru came up with his suggestion to set up a Commissioner General's office in Washington D.C. under his leadership with three persons of his choice to comprise his staff. I was one of those he chose; and I found this opportunity difficult to resist. Bibi and I had met in Washington and the idea of beginning our married life there was exciting.

There was one hitch. B.K. Nehru wanted me to start in Washington right away—around June or so. That meant I had to come back to Delhi to get married in November. Nehru did not think the Government could pay for my passage and offered to get us married in Washington, but this was unacceptable to our families. The impasse was broken by no less a person than Panditji himself, who sent for me.

The conversation ranged over a number of issues for nearly thirty minutes. He wanted to know what I thought was wrong with India and what could be done to bring about another burst of energy in the country such as existed during the struggle for independence. I do not remember what I said, except that I suggested some form of compulsory national service to which his response was positive.

Suddenly, Panditji's eyes became mischievous and he said, 'So, you are getting married. Good. You have kept it away too long. But what is this I hear about your wanting to go to Washington? Our work is here in India, not in Washington. Sometimes, we may have to go there to talk to people. Bijju (B.K. Nehru) tells me he wants you to go there. Go there by all means. Find out what the work is, what it requires. Then come back, travel in India and equip yourself fully before you go back for some time. How can you represent India unless you have seen some of it well? Also, I hear some World Bank meeting is taking place in Delhi in November. You must come back and attend it. How can you

represent us there when you are not attending this meeting in our own country?'

I was dumbfounded. Here was the Prime Minister of India talking to you like a friend. Then suddenly obliging you without letting you feel any sense of obligation—no condescension, no admonition, no thanks asked. There was no question of thanking him. I could only look at him in gratitude, just managing to keep the tears away.

The Commissioner General

The Commissioner General's office was set up in Washington D.C. in the summer of 1958 and I spent three or four months in that city before returning to Delhi for the annual meeting of the Bank and the Fund. Apart from B.K. Nehru, the two other members were Govindan Nair who became Minister (Economic) in the Embassy and C.S. Krishinamoorthy who became Nehru's alternate on the Board of Executive Directors of the World Bank. I was made the alternate director for India on the Board of the Fund. Our main task was to prepare the ground for massive concessional aid to India from the US and its rich allies as well as from international institutions. In this, the Commissioner General's office was immensely successful. Nehru has himself told the story of this chapter in India's economic history.[1] All I can do here is to recount some of my own experiences during the time I was in Washington.

By the time I arrived in Washington in the summer of 1958, the US had already set up the Development Loan Fund (DLF). The story of the Fund is not often told. But it shows how responsive the US was at that time to the needs of developing countries like India. The Fund was set up in the latter part of President Eisenhower's administration; and it is not too much to claim that in large part, it was a response to India's need for soft or concessional loans. The inspiration for it, I believe, came from Douglas Dillon who was in the State Department under Eisenhower. Kennedy included him in his own administration. Dillon's idea—undoubtedly supported by Senators Kennedy and Cooper—was to borrow from the PL 480 legislation: if wheat could be sold for

rupees, so could loans be given for development and made repayable in local currency. I remember calling on Dillon when the DLF legislation had just been passed and asking him to what use the rupees would be ultimately put. I mentioned that the legislation was not very clear on this point. His reply was, 'Mr Patel, I do not believe in answering questions which have not yet occurred to our Congressmen. If they ask it we will find some answer.' Another lesson in diplomacy. People like Dillon and Cooper and Kennedy knew that ultimately the rupees—whether PL 480 or DLF—would have to be written off or returned. I remember telling Patrick Moynihan (in 1972) that his first job as US ambassador to India should be to write off the rupees. As an economist and a statesman, he knew there was no other alternative and that not doing the needful early enough could only create unnecessary misunderstanding. Moynihan performed a lasting service to Indo-American relations by removing the bulk of these rupees from the US books.

Govindan Nair and I were literally on the doorstep when the DLF opened for business. Ours was the first application to be entertained; and Perry who was in charge at the DLF could not have been more helpful. In fact, both the US and we were learning how to give and service concessional development aid; and we learnt much from each other.

During that summer or early autumn, there was an important conference on India at the Mayflower Hotel. Apart from Kennedy and Cooper, there was another key speaker: Richard Nixon, Eisenhower's Vice President. Advocacy of aid to India thus was on the bipartisan agenda; and the US was mainly concerned then with making this effort international by persuading others, particularly France, Germany and Japan, to join. British support was rightly taken for granted—and let it be known that the British were also actively behind these efforts.

My main job during those months was to brief various persons in the Bank and the Fund and some in US administration and Congress about what we were trying to achieve in India and to remove some of the misunderstandings. Kennedy had already announced support for India, and it was known that he had presidential ambitions as well as potential. I was to help his assistant

Fred Holborn in writing speeches for Kennedy and in briefing others who mattered on the Hill. I remember one occasion when Fred and I were working in Kennedy's Senate office. Fred asked me to sit in Kennedy's chair, saying someday it will be the presidential chair. I did sit on the Senator's throne, if not on the President's!

It was early in 1959 that I assumed charge at the IMF as alternate executive director. The Executive Director, B.N. Adarkar, took care of most of the work in the Fund. But I knew the Fund well and was interested in its work and was happy to be able to have a ring-side view of what was happening.

On the aid front, my main activity continued. Only the speeches I wrote for Nehru increased greatly in number and range. I must admit that I was more than amused when many of these appeared in a couple of volumes entitled *Speaking of India* by B.K. Nehru. But that was all in the game, so to speak. Nehru did later credit one of the speeches to me: it was on India's Vedanta philosophy for which he was chided by his father who asked him not to dabble in matters he did not understand. The rest were neither disowned nor acknowledged.[2] But the same was true of many other speeches I wrote;[3] and I sometimes wonder whether I was not more valued then as a speech writer than as an adviser. I can say in all honesty that when my time came, I could not bear to read out a speech written by anyone else! More seriously, whether it is speeches or reports or policy briefs or memoranda or minutes of discussions or submissions to donors or parliaments, the ability to draft quickly and hopefully clearly, if not elegantly, is a great asset in public service, nationally or internationally.

Speeches apart, a lot of effort went into clearing misunderstandings. The two most common criticisms of Indian economic policy then related to our 'socialism' or antipathy to Indian and foreign private enterprise and 'deficit financing' or inflation. Often, the criticism was carried over as opposition to aid to India. To a large extent, criticism of our policies of controls and public sector predominance was justified; and it was not easy to defend all we did: the best we could do was to argue that things were changing and more and better quality of aid would assist the process of change, for example, by enabling us to reduce the severity of

import controls. In this area, we were defending something in the US while pleading for their reform or removal in Delhi. It was not a one-way street: with the Bank as well as the US administration—if not with US private industry and trade—there was much mutual give and take and accommodation for each other's point of view.

As far as inflation or deficit financing was concerned, the situation was rather different. Our record in this regard was good and certainly better than that of most developing countries. But there was much misunderstanding of our budgetary position, much of it spread by economists like Shenoy[4] who wrote to all and sundry about the need to cut off aid to India as it was encouraging deficit financing and similar evils. He was not above distorting or misreading facts; and his words carried weight with economists like Peter Bauer in the UK, and the Chicago School in the US. The new Managing Director of the Fund, Per Jacobson, was also singularly allergic to deficit financing. It took much effort to explain the realities of the Indian budgetary situation to every one.

Two budgetary items created special problems. According to some, both PL 480 and drawings on the Fund were inflationary as they added to deficit financing and the purchasing power of the State. The logic was difficult to understand. PL 480 supplies were not given free to the Government. The Government purchased the wheat with rupees, so that this purchase entered as a governmental expenditure. When the wheat was sold, the budgetary receipts increased, so that in purely financial accounting terms, the purchase and the sale balanced each other and the budget deficit remained unchanged. In real terms, there was, in fact, disinflation as the rupees credited to the US Government were largely not spent, whereas wheat sales did withdraw some purchasing power. One could argue that keeping this in mind, the Government could increase its developmental expenditure. But this would be reflected as an additional deficit unless it was matched by additional mobilization of resources. It was certainly true that PL 480 supplies helped increase developmental expenditure. But it was absurd to argue that they added to deficit financing or were inflationary. The same was true of Fund drawings where, too, the foreign currencies were purchased and not just given.

Somehow, these simple points were not grasped by the likes of Bauer or Shenoy—and I had difficulty explaining them to my friend Harry Johnson at Chicago. When he saw the point, he asked me to write it up and circulated my article[5] and may even have managed to publish it somewhere.

The US steel industry was peeved by India's refusal to allow a private US steel plant to be set up, and at their instance, Peter Bauer wrote a short pamphlet criticizing India's economic policies and advocating stopping of all aid to India. I wrote a rebuttal and it was agreed between the publishers and us that Bauer and I would have a public debate on this pamphlet on the radio. But when the time came, Bauer—or his publisher—walked out of the deal.

Not all, however, were deaf to our arguments. Per Jacobsson soon understood the issue as well as the figures. Another sympathetic person was Eugene Black,[6] a perfect gentleman if ever there was one. Shenoy sent him many notes making one point or another against India, and he used to send them on to me, saying that he would like to discuss the matter with me some time. I was ready with my rebuttals. When Black finally did send for me, it was simply to tell me that he knew Shenoy must be obsessed—why else would he write so many angry notes in the same vein? He had sent them to me in case I had not seen them. He went on to add that while Shenoy was entitled to his views, he could not understand how anyone could carry on a vehement propaganda against his own country in another country. Pride and a sense of duty and propriety were not altogether absent in the world of US finance then; and I think Black was the best friend India had in the US at that time. His departure from the Bank ushered in a very difficult and cantankerous chapter in the long and on the whole very cordial and mutually fruitful relations between India and the World Bank.

*The Aid India Consortium**

The climax of the Commissioner General's achievement came with the first meeting of the India Consortium in 1961. What this

*New York, 10 January 2000.

meeting signified was that the Bank and the Americans had decided to put their weight behind mobilizing concessional aid to India, that they had succeeded in bringing around a number of other countries to their point of view and that a mechanism was created whereby India's needs would be assessed annually and commitments of aid—hopefully over a number of years—made by the various donor members at these annual meetings. It is difficult now for people to appreciate what a tremendous achievement this was. Subsequently, many other countries, including Pakistan, benefited by India's pioneering efforts; these efforts in fact were to continue till an international agency for concessional development aid was created.

The outcome of the first Consortium meeting was extremely gratifying. Our demands were matched dollar for dollar with commitments—although the actual signing of loan agreements was to take place in due course. If I am not mistaken, some initial non-project aid was also available. In the event, not all commitments were fully honoured in letter and spirit; and some countries like Germany, Italy and Japan were reluctant to budge from their preferred mode of suppliers' credits. But they were competitive; and over the years, each improved the quality of aid as a result of emulation of others or arm twisting by the US and the Bank.

It must be admitted that the election of Kennedy as President greatly facilitated our efforts. His advisers, mainly from MIT, had been solidly behind us and we had worked hard to gain support from the academics at Harvard too. Rosenstein-Rodan, Max Millikan, Walt Rostow, J.K. Galbraith, Senator Moynihan and many others were our best ambassadors. I had visited Cambridge often (and even Chicago once) to give lectures on India or to participate in seminars. Some younger MIT or Harvard economists had begun to stay in Delhi for months at the behest of the Ford Foundation; and this fruitful presence continued for many years. One Wilfred Malenbaum from MIT was the first to arrive in Delhi under the Ford initiative in 1956 or 1957; and although he was a lightweight in expertise and influence, he did make our case better known where it mattered. He was a bit abrasive and not always

supportive of our policies. But his heart was in the right place and he was hospitable to us during our several visits to Cambridge. To the seniors—Rodan, Millikan and Rostow at MIT—one cannot really be grateful enough. They had expertise as well as influence, and were generous and warm-hearted in personal relations almost to a fault.

While our efforts were mainly focused on Washington, we did not overlook the United Nations in New York. B.K. Nehru or myself regularly visited New York to take part in the debates in the Ecosoc (Economic and Social Council of the UN) and we carried on the battle for SUNFED, a 'Special UN Fund for Economic Development' which would make the UN a pioneer in concessional development assistance, both technical and capital. Our major triumph was to get the resolution on 1per cent of GNP as aid target for the rich countries passed, with 0.7per cent as concessional aid; and the passing of this resolution has been a major landmark in the history of foreign aid. While the target has never been achieved, it has served as a benchmark and has been useful at least in the case of some countries, such as Sweden and the Netherlands, which have increased their aid effort even beyond the target. Even in the US it could not be brushed aside. Ultimately, it was the pressure generated in the UN which persuaded the US and others to accept a lesser evil, that is, the International Development Association under the leadership of the World Bank. But the main idea was accepted: concessional aid was necessary for developing countries. Later, this idea was to extend to trade and to Fund transactions including creation of reserves, and again, the debates and discussions in the UN (including the UNCTAD) were a contributory factor in this change.

The IMF

A word may be said at this stage about developments in the IMF where I served as Alternate Director. I do not remember much, except that murmurings of monetary reform were already around even then. Robert Triffin was canvassing his ideas against fixed exchange rates (mainly the scope for one-sided speculation) and

the dollar standard. In the Fund, the idea of created reserves officially first came up during the discussion on France. The French had contended that they needed to build up their reserves. I remarked at the board meeting that the French were not alone in this: all countries rich and poor, thought their reserves were inadequate. Since the US was not prepared to continue large balance of payments deficits to provide others with dollar reserves, where were the additional reserves to come from? The case for created reserves was obvious. This point was picked up by Lord Cromer, the British Executive Director. We were, of course, far removed then from the idea of the Fund creating reserves outside the quota system—and very far indeed from creating reserves for 'a substitution account' which would end the dollar standard. But the ideas were in the air.

Towards the end of my stay in Washington in 1961, I had to assume charge as the Executive Director for a few weeks as Adarkar had to leave for India and his successor, Anjaria, could not come for some time. This interlude saw a rather remarkable drawing by India—I believe of some 250 million dollars—from the Fund. As soon as I assumed charge as Director, I realized that our reserves were declining fast and that we may need a Fund drawing. I cabled L.K. Jha who immediately wrote back that I must urgently arrange for a drawing. I contacted Per Jacobsson at his residence at the Wardman Park Hotel one Saturday evening as I knew that he was leaving on a European tour that weekend. He invited me to lunch on Sunday; he was leaving that afternoon. Jacobsson needed no persuasion and he was happy that I had seen him before his European trip as the main opposition was likely to be from France and Germany and not from the US or the UK. The price I had to pay for his goodwill was to patiently hear his humorous accounts of his audience with de Gaulle and other world leaders, all the while giving him company in his lavish drinking of good scotch. He was none the worse for the whisky; and he had garnered all the support we needed when he returned from Europe.

I cannot recall what was going on in India in terms of economic policies. I presume this was a quiet period when we were trying to salvage as much as we could of the Second Plan. In fact, the Second Plan was rephased after 1958–59 in the light of the

foreign exchange crisis. Much depended on foreign aid, so that, in a way, we in Washington were at the centre of things. Morarji Desai visited Washington in connection with Bank–Fund meetings and he did his bit to advance our cause. His own aversion to deficit financing was music to Jacobsson's ears and the two—unexpectedly—got on very well. B.K Nehru even persuaded the Minister to let him serve liquor at parties in his honour. Morarji's only condition was that the Indians would not drink. He was shrewd enough to know that we would arrive early and have a drink before he came; and the usual pattern was for everyone to come early and for Morarji to come deliberately late whereupon fresh drinks were not served (not in the same room anyway). On the whole, he got along well with officials in the Bank, the financial community and the US administration. He trusted his advisers, used the briefs well and had a sense of humour which we had not suspected.[7]

The most memorable visit during this period was that of Panditji at the invitation of Kennedy. In his inaugural address, Kennedy had mentioned Panditji; and he was anxious to have talks with Panditji on world issues—not just Indo–US relations. In many ways, the visit was a disappointment. Apparently, Panditji was listless and non-communicative most of the time. In retrospect, he was ill and tired and was probably on medication which made one listless. But Kennedy certainly was disappointed and may have wondered whether some innate anti-Americanism was in evidence.

On a personal note, Panditji once again floored me when he met some of us from the Indian embassy on his arrival at Blair House. He was obviously very tired after a long journey. But as soon as Mrs B.K. Nehru introduced my wife to him and said she had deserted me in order to get a higher degree from Harvard, Panditji's face lit up; he literally lifted my wife from the floor, swung her around and introduced her to others as a brave girl, adding that married life could wait but it was important for women to take every opportunity for higher learning. Perhaps it was an attempt to shake off his boredom and fatigue. But he did win a young woman's heart!

Towards the end of 1961 I returned to India to become the Chief Economic Adviser in the Ministry of Finance as Anjaria's

successor. I also assumed his charge as Economic Adviser to the Planning Commission—something which neither the Commission nor I liked and I shed that charge as soon as I decently could. My friend, K.S. Krishnaswamy, became the Economic Adviser in the Planning Commission. When I took leave for one year in 1964 to join the Delhi School of Economics, the Planning Commission was no longer its old lively self except for Pitambar Pant's division on long-term perspective planning where many bright economists came to work and with whom—as with Pitambar—my wife and I developed warm personal and professional relationships over the next few years and more. The eleven years from the beginning of 1962 to the end of 1972 which I spent in Delhi have undoubtedly been the most hectic in my life. If we were not always right, we were certainly highly motivated and not sparing of ourselves in any way. Those were years of commitment and we worked as a team, remained friends at home and in office and had a rewarding and enjoyable time in every way. Those who know Delhi only after the early seventies cannot have any idea of what bliss it was to work together in friendship and mutual respect and with a sense of pride and purpose.

Endnotes

1. *Nice Guys Finish Second*, B.K. Nehru, Viking, Penguin India, 1997.
2. My copy of the book presented by B.K. Nehru, however, bears the inscription: 'To the real culprit from the putative father. BKN. 4.9.63.'
3. A volume also appeared entitled *Speeches of T.T. Krishnamachari* which had similar parentage.
4. He argued that PL supplies to Government of India added to inflationary pressure and should be stopped. The general expert view was that quite the contrary was the case.
5. Unfortunately, I have no copy.
6. Eugene Black was the president of the world Bank at the time.
7. At a dinner in my place, he sat on the sofa and gently knocked his head against the wall. After a while he asked what was behind the wall. When I informed him that there was a stair-well, he said: 'Thank God. There was so much resonance that I wondered whether there was a big vacuum in my head.'

4

The Chief Economic Adviser 1962–6

When I returned to Delhi in December 1961 as Chief Economic Adviser to the Ministry of Finance and Economic Adviser to the Planning Commission, I succeeded J.J. Anjaria—but not quite.* As L.K. Jha explained to me, this position was that of an Additional Secretary with pay of Rs 2750 per month. Considering my age (37), it would be easier if I accepted the same responsibility, but a lower pay and status: a pay of Rs 2500 per month and the status between that of a Joint Secretary and Additional Secretary, a kind of leader of one caste and an outcast from a higher one. I had faced this situation in 1954,[1] and was to face it again in 1967; and my response on all occasions was the same. I would be more than happy with whatever was on offer as long as my responsibility was clearly defined. Even in the Fund, when I was made an Assistant Chief in supercession of a senior person, my salary was fixed at a lower level despite the fact that I was given higher responsibility. There is, in my judgement, much to recommend in such a system of overlapping pay scales for different levels of responsibility. It permits promotion by merit while recognizing the financial claims of seniority. I doubt, however, if my colleagues in the Indian Administrative Service were guided by

*London, 13 May 2000.

any notions of principles or sound policy. L.K. was simply finding a way out of a dilemma: to give me what he thought I deserved and the Ministry what it needed without offending his ICS or IAS colleagues too much. I have at least the satisfaction that having broken the ice, I made it easier for economists in future to occupy similar posts without similar obeisance to tradition.[2]

That I should also succeed Anjaria as Economic Adviser to the Planning Commission came as a surprise to me, and this double charge was not much to my liking. I had felt for quite some time that the Planning Commission—like other Ministries—should have an independent adviser of their own choice. But Deshmukh's tradition of making the Ministry of Finance the purveyor of all economic wisdom still commanded some support under Morarjibhai.

The eleven years that followed (1961–72) have been perhaps the most active and rewarding in my professional life. But surprisingly, my memory of what happened during the period is vague. A few important episodes stand out in my mind. But I have only a faint recollection of what happened year after year. Perhaps absorption in day-to-day routine but demanding responsibilities leaves little mark on one's mind. In my case, most of these years were spent in economic diplomacy: negotiating agreements and signing them, shuttling from one capital to the other, making speeches, preparing presentations for visiting teams or for international conferences such as the meetings of the Aid India Consortium. All these were exciting but all-absorbing jobs and had to be combined with work relating to the Budget, the Parliament and membership of a number of Committees and Commissions. But not much of it leaves a sharp impression and provides material for an interesting story. What follows thus is not in any sense an economic history of these eleven years in India. It is simply some highlights of one man's involvement in it.

On assuming charge, I got immediately involved in the preparation of the 1962 Budget: the proposals, the preparation of the Economic Survey and the drafting of the Budget speech. Being an election year, the Budget was a routine one; and the only noteworthy thing was a trip I had to take with Morarjibhai on a special

army plane to Somnath temple so that I could get his approval in time for the Budget speech. They were all so busy with the elections that I could get enough time with Morarji only if I accompanied him to Somnath where he had to attend a meeting of the Temple Trust as its Chairman. Much of the speech, in fact, was written in the temple guest-house!

*The Chinese War: Defence and Development**

The Budget was soon overshadowed by the Chinese War. It is difficult now for people to imagine what a great shock and surprise it was and how it demoralized everyone when Bomdilla and other army posts fell to advancing Chinese armies. They retreated on their own volition as swiftly as they had cut through our own defences. Their retreat was as much a slap in the face as their advance. If what we felt as Chinese ingratitude and treachery were difficult to stomach, the humiliation of 'being taught a lesson', as the Chinese put it, was even more difficult to bear.

One consequence of the war was that it brought India and the US closer together for a while. President Kennedy was genuinely interested in helping India militarily. But we were anxious to preserve our neutral image and were wary of US intentions. There was already talk of US pressure on us to settle the Kashmir issue. I remember a meeting when some US Senators and Congressmen called on Morarjibhai at his residence just hours after we had received information of the fall of Bomdilla. The meeting in fact was one long monologue when the American legislators harangued us, mostly about Kashmir. To say the least, this was a most insensitive performance when what we needed were some words of comfort rather than lectures on matters which were far from our minds at the time. In fairness, it must be said that the Minister in the US Embassy in Delhi, Taylor, who was present at the meeting, made it a point to return soon after to apologize profusely for the very bad manners of his countrymen. Taylor was a Republican and was

*London, 14 May 2000.

known for his very conservative views. But he was also an affable and sensitive person and his conscience as a gentleman made him take this rather unusual and prompt step. It is this essential sense of decency of most Americans that we often tend to discount in India.

Another by-product of the Chinese War was the 'Defence and Development' slogan and the attempt to translate that into action. The Third Five Year Plan had begun in 1961. The sad experience of the Second Plan had reduced the glamour of planning and diminished the ardour for boldness and novelty. Even Pitamber Pant, the very able and adorable and indeed lovable disciple of Mahalanobis, had begun to speak of 'Basic Needs'. Once again, employment and better distribution of income were emphasized as important objectives. Mahalanobis himself chaired a committee on distribution of income. What one might call the 'humanitarian' side of socialism was thus emphasized once again in place of the grandiloquent one. It is worth emphasizing that since the beginning of planning we have been concerned about the human aspect of development—something that the enthusiasts of the recently promoted Human Development Index tend conveniently to forget. One has only to read our earlier Plan documents to appreciate this. We were aware of the QLI—the quality of life index—long before the indexing of human development was discovered by the UNDP.[3] The UNDP popularized and elaborated it when the time was ripe. It may be ironic, but it is true that the World Bank used to criticize us and to compare us unfavourably with Pakistan because we were not focused sufficiently on growth in the fifties and sixties and were concerned too much with equity. In the seventies, we were criticized for the opposite!

Truth to tell, the enthusiasm for planning and bold plans which abated then never really caught a second breath in India. The façade was kept up with input–output models, perspective plans, even superior optimizing models and so on. But the substance of financial planning virtually from year to year with all its opportunistic—or realistic and practical—overtones dominated the policy platform. In the larger historical perspective, planning will be judged to have had a life of barely ten years in India. What endured, alas, was the scarcity mentality and the consequent licence–permit raj; and what was revived later was the ideological face of socialism with its penchant for nationalization of the means of production or at least, the public occupation of the commanding heights of the economy. The one essential function of distributing financial resources between the Centre and the states which the Planning Commission has continued to perform could well have been left entirely to the Finance Commission.

To imagine that even the modest developmental effort then underway could be abridged in the interest of better defence preparedness was inconceivable. But in the climate of public humiliation, the additional defence effort undertaken was of such a magnitude that it was not easy to absorb it without further pressure on prices and balance of payments—and, over the medium-term, without a cut in public investment. Patriotism does not always square well with economic common sense; and so it was to be on this occasion as well.

Redistribution—A Digression[4]

There is a general moral in this. How much change in the distribution of income can we make in the short run by means of economic policy? The answer is, unfortunately—not much, not even in the medium term. If defence and development have to go together, there has to be a shift in the proportion of national income mobilized by the government. This means raising revenues, by and large, by indirect taxes, including pricing of public services, as direct taxes are generally high anyway and tend to be avoided and evaded beyond a point. But large increases in indirect taxes or prices of public services (including reduction in subsidies) are not accepted meekly by the people. They fight back—by demanding and getting higher wages and raising prices in general. Besides, as input–output tables would remind us, large changes in prices in major sectors soon spread to all sectors. In the second round, the increase in public revenues is virtually balanced by increases in public expenditure. An attempt to recapture the lost budgetary

improvement meets a similar fate; and all we get in the end, is another upward twist of the inflation spiral.

This is not to suggest that the share of the public sector in the total economy or the share of savings in national income cannot increase over time. This has happened. But it is almost entirely the result of voluntary responses to increases in real incomes and wealth which are a product of improvements in technology and productivity. The share of the public sector in national income and expenditure will rise over time with growth in incomes if direct and indirect taxes are set in a progressive mould.[5] Even without a growth in incomes, a lot can be achieved by better collection of taxes and bringing within the tax net those who have managed to be out of it. Some reduction in public expenditure is perhaps more feasible. But such gains through tax administration or tax coverage and expenditure economy cannot be repeated from plan to plan. It is growth—and not redistribution by policy—that primarily increases the rate of savings and the share of government in total expenditure.

I remember the renowned Japanese economist Saburo Okita telling me that Japanese rates of growth were not high because of high Japanese rates of savings. It was the other way around. The driving force comes from productivity. It is that which raises growth rates as well as savings rates. It may even provide a basis for increasing the role of the government if the tax system is progressive.

The point is a more general one. There is often confusion between microeconomics and macroeconomics. Microeconomics applies to small changes taking place over a very small part of the total economy. In so far as economic policy makes small changes over a small sector of the economy, it can bring about changes in relative prices or incomes and in the allocation of resources—small changes. But the temptation is to extend the argument to large changes over large areas of the economy: something like an attempt to shift the distribution of income in favour of the public sector by higher taxation, or to shift the distribution of income in favour of workers by minimum wages or compulsory benefits for workers, or for that matter, to try and improve the trade balance by a large devaluation. One ends up by having only a small effect, if at all—

thanks to resistance by other sectors and the interdependence of different parts of the economy.

Historically, there is little evidence of any significant and durable improvement in the distribution of income in favour of wages and away from profits in most countries—again, abstracting from revolutions and rearrangement of property rights which have their own short-term and long-term dynamics. This is not to say that the condition of workers does not improve over time. It does: as a result of improvement in productivity. And it is also true that legal and other efforts to improve the condition of workers through minimum wages, education, training, safe conditions of work, better health facilities and the like have a part to play: by increasing productivity, stimulating growth and, in the process, increasing both real wages and real profits.

The case for international trade—for a certain allocation of resources to improve the share of such trade in the economy—is on a somewhat different footing. It is almost axiomatic that trade follows comparative cost advantage. That different countries have comparative advantage in the production of different commodities and services is also a fact of life—even if the centres of such advantage and disadvantage are more man-made than God-given, more historical than eternal, and capable of change and influence. It follows that international trade is beneficial all round and that it makes sense to make it as free as possible.[6]

This does have a bearing on how we allocate resources. But it is too simplistic to say—as is sometimes done—that resources should be diverted to the trading sectors as against the non-trading sectors. Without an efficient infrastructure like ports, roads and power, there would be poor growth and poor exports. It is as well for us to remember also that efficient and adequate infrastructure facilitates both exports and imports: the gains from trade ultimately arise from the ability to import (and consume or invest) what you want at least cost in terms of resources. One cannot neglect imports and lavish all of one's attention on exports. Widening and deepening the area of foreign trade also resolve themselves ultimately into a general search for higher efficiency. Normally, in

a market economy, the natural instincts of traders and investors will lead to right decisions which would more recognizably be reflected in opportunities for profitable trade and investment. But what increases the proportion of international trade in the national economy is freedom of trade and efficiency all round. There is a fundamental fallacy in talking of export-led growth as much as there is in pleading for import-substitution. It is general efficiency and freedom that spur growth and enhance the role of both exports and imports.

It is when we try and interfere by large changes in exchange rates that some confusion arises. Apart from the fact that large changes do not stick (monetary changes do not translate fully into real changes), there is unreality in the notion of shifting resources from the non-tradeable to the tradeable sector. Notice that one does not justify a change in the exchange rate in terms of shifting resources from the import-competing sectors to the export sectors. That would produce no improvement in the balance of payments. But what are the non-tradeable sectors? The fact that power plants, ports, roads and railway cannot be exported or imported in their final crystallized configuration, does not mean that they are divorced from foreign trade or from the so-called tradeable sectors in the short or the long term. And he would be a poor planner who starves the social or economic infrastructure for the benefit of the balance of payments. I cannot help feeling that this whole notion of tradeables and non-tradeables is a red herring and is an example of the fallacy of misplaced concreteness.[7]

Again, small changes spread over small sectors can stick, and work. That is why the infant industry argument—justifying export subsidies and import duties—has validity if we limit them to small areas and small amounts and short periods. The allocative effects would be small, but real in the sense that they are likely to endure, the more so because they are in line with the curve of rising productivity which after all is postulated in the infant industry argument. If there is learning by doing, the protection would be needed only for a short period and should be withdrawn after a while. But protecting everything is equivalent to protecting nothing.

For similar reasons, a very large devaluation would have only small lasting effects.[8]

All this has nothing to do with the desirability of keeping in step with inflation rates in other countries with whom one actively competes. But again small and frequent changes are better than large and infrequent ones; and better still are policies to counter inflation. Naturally, if one has not made small but frequent desirable changes for a long time, it is better to make a large change sooner or later than make no change at all. While an overvalued exchange rate may not shift internal resources from the so-called tradeable to non-tradeable sectors, it does reduce your share in international trade and thus your share in the international division of labour which retards the overall dynamism of your economy.[9]

*Gold Control and Gold Bonds**

An important by-product of the Chinese War was the Gold Control Order. The question of reducing the drain on foreign exchange by reducing smuggling had been under discussion for many years; and it was felt that with the upsurge of patriotism in the wake of the Chinese War, it may be feasible to make a frontal attack on the demand for gold in India. I do not know who originated the idea of Gold Control. But I was certainly one of its most ardent proponents. I had reason personally to bemoan the Indian passion for gold jewellery, which has been sanctified by custom into a social duty. The necessity to spend on jewellery especially for a daughter's marriage has ruined many poor and even middle-class families. Perhaps during the uncertain centuries when internecine conflicts, wars and banditry were so common, it made some sense to idolize gold. Because of its large value in small amounts, standardization and capacity to be stored on one's own person—and to enhance personal beauty to boot—it was a desirable store of value and a safeguard for leaner times. Even then it was perhaps childish to

*London, 15 May 2000.

think that flaunting all your wealth in one form to advertise and enhance your beauty added to the safety of your wealth or to your personal security in adverse times. And any male prejudice that this was a feminine foolishness would be misplaced as men were not averse to wearing jewellery in those days, and valued gold even more in all forms as wealth.

By the middle of the twentieth century, however, the attachment to gold had become more of a social tyranny than a sensible way of storing wealth. Many parents, we assumed, would be happy if this social burden was partially lifted by setting up a new trend and fashion and indeed a legally enforced norm in favour of ornaments with lower gold content—from 22 carats to 14 or even 8 in due course as is the case in most western countries. The idea was that the legal norm would soon become socially acceptable as it answered the social need to reduce expenditure on marriages. Nationally, any reduction in demand for gold would be a great saving in much needed foreign exchange. The earlier step of withdrawing Indian currency from the Gulf had not proved effective. Other forms of financing the traffic in gold had developed: underinvoicing of exports and overinvoicing of imports and diversion of remittances to the black market. A reduction in the demand for gold would strike at the very root of the problem. And at a time when 'defence and development' was the order of the day, it was opportune to take a bold step to attack this age-old malaise.

How this reasoning was translated into the Gold Control Order is more than I can say. But it was felt that if the making and selling of jewellery above 14 carats was to be made illegal, gold trade and goldsmiths must be licensed and submission of accounts of all gold received and utilized was to be enforced. Since gold smuggling was illegal, what could be legally accounted for was gold purchased as old ornaments or supplied by official agencies. There were other aspects of the Control such as the control over gold refining on a large commercial scale and declaration of any addition to the individual possession of gold in non-ornament form. But the substance and core of the Order lay in the control of the trade and manufacture of gold ornaments.

And it was on this central front that the Gold Control enterprise failed, and failed miserably. Making of gold ornaments was carried out in thousands of small establishments in far-flung villages. It was impossible to licence or monitor this vast unorganized industry or to divorce it from the movement of smuggled gold. The making of 14 carat ornaments also required new equipment and technology, which were beyond the reach of most small goldsmiths. The result was that a large number of goldsmiths were thrown out of employment. Since this was patently unacceptable, they had to be rehabilitated and given alternative jobs—a herculean task. Before long, self-employed goldsmiths were allowed to repair and remake ornaments of more than 14 carat purity. This opened a big loophole which made it difficult to implement the Order. In stages, the Control was relaxed and allowed to remain an ineffective adornment on the statute book until at last it was given a decent burial. Truth to tell, there was little enthusiasm and support for Gold Control in the Congress Party itself.

What was even more disappointing, the measure met with almost total social opposition. Those who were supposed to benefit—impoverished parents of marriageable daughters—raised no voice in its favour. After all, who wants to advertise one's poverty or helplessness? But there were more genuine reasons for social and political opposition. The administrative complexity of the measure was truly great. The plight of the goldsmiths was real. The social custom of giving gold jewellery to girls at the time of marriage was intended to give some economic security to women who were often denied their share in property or even alimony or pensions. There was also the paramount question of individual freedom: what right has the Government to interfere with people's personal preferences? Is it such a crime in a poor society for people to indulge in such small luxuries? Pandit Nehru in his *Autobiography* had justified the poor peasant spending large sums of money on festivals and marriages. For those whose life is blighted by abysmal poverty and who do not get two square meals a day, is it a crime to splurge once in a while and eat and drink to one's heart's content? My sister-in-law put it very vividly: 'Bhai, unlike

some of you, we do not travel to London or Paris which also costs money and foreign exchange. If we prefer to remain in Baroda and buy some gold for our children from time to time, how is it that we are to blame, but you are not?' My father—who I thought might sympathize with the Control—simply said, 'Pothi maana ringana' (bookish ideas).

Much as I was personally agitated and emotionally involved in the issue at the time—as can be gauged by my subsequent behaviour to which I will soon refer—it has to be admitted that the Gold Control was misconceived and should never have been attempted. The aims were admirable. And perhaps it can be argued that a better control could have been devised which would have been administratively feasible and which would have achieved results over time, albeit more slowly. But that is for some future researcher to explore. What seems to be the moral of the story is our familiar friend: only small changes, improvements, shifts towards the good or the better, are possible. The ambition for rapid or large changes proves counterproductive.

One cannot give up the ambition to correct social attitudes by legal action. Can we fight *sati* and infanticide and untouchability without any legal prohibitioin? Some crimes, whether individual or group or social, may have to be dealt with firmly even if the initial success is limited. But legal action can succeed when it leads in the direction in which public opinion and public choice are already moving or can be made to move by argument and information. One has always to remember that public choice can assert by evasion. Perhaps there is a degree of coercion which can overcome even rigidly held views. It is such thoughts which make some people still hanker for the Emergency. But even if this line of thinking is right, who would want to travel on that road which abounds in even greater dangers?

There is also the moral that economic policy is not just about economics. It is about history, sociology, politics and psychology as well. When wrong policies have accumulated—like an overvalued exchange rate—one can perhaps dismantle them swiftly, particularly when public opinion is already prepared for it. That is

why controls and licensing systems can be demolished rather speedily. But even here one has to recognize that long-entrenched economic policies, even when faulty cannot be withdrawn without adversely affecting some sections of society. And not all of them may have been rent-seekers or unworthy profit-makers. Their interests may demand compensating action or a slow reversal of policy or both.

Not all the demand for gold comes from the jewellery trade. Gold is also hoarded in bars and biscuits as a store of value or as investment. In times of crisis, and even in normal times, there is the temptation to think that this gold can be mobilized for public purposes by appropriate policies or incentives. Many such gold mobilization schemes have been tried in India—and one was tried soon after the Chinese War. For patriotic reasons, many people surrendered their jewellery or hoarded gold in exchange for gold bonds. But on the whole, this scheme too was a flop. The basic fallacy in all gold mobilization schemes—whether gold bonds are redeemed in gold or in money—is that they all make the purchase and holding of gold more attractive in the long run. If you can have your gold and earn income from it and avoid storage charges, you will buy more gold than otherwise over a period. One can even argue that a successful gold bond scheme would be even more harmful as it would generate the expectation of the scheme being repeated, thus providing even greater incentive for fresh purchases of gold.

Gold hoarding can best be tackled by better savings schemes and greater protection to investors against frauds. A more stable price regime would also help by safeguarding better the real value of monetary savings. There is ample historical evidence that gold has seldom been a good investment over the long run. My hunch would be that such gold as is now held in bars and biscuits is largely for the purpose of hoarding black wealth in a convenient way: it costs little to store and is less conspicuous than marble houses or a flamboyant lifestyle. In so far as this is true, a gold bond scheme can succeed like any other money-laundering scheme which offers immunity regarding previous crimes. But by the same token, it facilitates the continuance of those crimes. The reason

why such schemes are popular and are resurrected every now and then is that politicians, administrators and businessmen all have one common interest: to regularize their ill-gotten wealth.

One last thought on gold: in these days when we talk of current account and even capital account convertibility, how long can we make the import of gold illegal? I have no doubt that sooner rather than later, gold imports will be freed, albeit with a duty. Even now, the fig leaf of what is permitted to NRIs and returning Indians is a confession that the King is already without clothes.

President Kennedy's death in 1963 was mourned in India, as in the rest of the world. There was no question that he had high regard for India and its leaders and at least understood our policies and preoccupations even if he did not always agree with them. His role in putting large amounts of concessional aid to India on a fairer and firmer footing cannot be denied. Nor can one fail to recognize how prompt his response was with military and other aid in the wake of the Chinese War. If he wanted India to succeed so as to demonstrate that the democratic way was better than the authoritarian one, there was nothing ignoble about such a motivation. Pandit Nehru's visit to Washington in 1961 had not been an overwhelming success; and many of us felt that Panditji should have gone to Washington for Kennedy's funeral. Instead, Morarji was sent and we had to pore over timetables to ensure that he reached there in time—which he did after an arduous journey just hours before the funeral.

Exit Morarji, Return T.T.K.

Little did we know that Panditji's refusal to go to Washington for Kennedy's funeral was not a matter of pride or pique. He knew what we did not—that he was dying. It would have been unwise for him to rush to Washington. I now think that the Kamraj Plan was also a response to this foreboding of the end and the desire to

influence the succession. It was felt even at that time that the Kamraj Plan was aimed at removing all possible challenges to Nehru's power. His prestige had taken a great beating as a result of the Chinese War, and there were rumours of a struggle for power. I doubt if there was ever any danger of a serious challenge to Nehru's power. The concern must be with succession—and I am reasonably certain that the Kamraj Plan was aimed specially against Morarji Desai. Morarji had been an important regional leader who had also been successful as Finance Minister. If there had to be a succession when he was in the Cabinet, it would have been difficult to set aside his claim.

In the event, T.T.K. returned to his favourite job in 1963. He had already been inducted a little earlier as Minister for Defence and Economic Coordination, a new Cabinet charge that was clearly intended to clip the wings of the Ministry of Finance. With T.T.K.'s return to Finance, the Ministry of Defence and Economic Coordination died a natural death. For the economists and civil servants in the Ministry, T.T.K.'s return was welcome: he was his old self in every respect.

Understandably, his first task was to review the Gold Control Order. I was made the member-secretary of a committee to review the order with L.K. Jha and several other secretaries as members. The Committee's recommendations were for several administrative changes and more rigorous efforts to rehabilitate goldsmiths but, for no change in the essential features of the order. I had to go abroad for some negotiations and I drafted the report at great speed; it was signed by all of us unanimously. On my return, however, I found that a postscript was added at the instance of the Finance Minister in which the other members of the Committee suggested a transitional modifications in the order, viz. to permit self-employed goldsmiths to repair and remake ornaments of more than 14 carats. Clearly, the intention was to give the Government a way out of the popular criticism concerning the plight of the goldsmiths. I was very unhappy that our report was tampered with in my absence. I knew that the change made was only a thin end of the wedge, and I decided I could not remain in the Government. The Delhi School of Economics was happy to have me.

I was apprehensive about T.T.K.'s reaction when I tendered my resignation. Instead, what ensued showed how fond T.T.K. was of me and how magnanimous he could be towards those whom he liked. He said he understood my point of view and even agreed with my views. But in politics, one has sometimes to compromise to salvage something. He would not come in the way of my decision. But he would prefer that I go on leave for one year and take a final decision at the end of it as I might not like university life. Meanwhile, I could keep my house so that my family was not suddenly disrupted. He had every intention of consulting me from time to time during the year, and this would be easier if I lived in New Delhi.

After that, it was difficult not to accept his offer. For the calendar year 1964, I taught at the Delhi School. Apart from teaching which did not take much time, I was able to attend to some long-neglected family duties. My father had died in 1963 and I had several things to take care of, including realizing his life insurance money. Not an easy thing. My youngest sister's marriage had to be arranged—again, a time-consuming task. She was married in the summer of 1964.

T.T.K. was true to his word. He dropped in often at our Pandara Road house. If I was not there, he would have a long social chat with my wife. If I was there, we would discuss something or the other. But mostly, he seemed to long for company where he could be himself. He insisted—much to the annoyance of some people—that I accompany him on his trip to Japan for the annual Bank-Fund meeting. It would be no exaggeration to say that he wooed me—and my wife. Above all, he kept alive my appetite for policy work.

Panditiji died the day after my sister's wedding in May 1964. Lal Bahadur Shastri became Prime Minister. We took a short holiday in Nepal. When we returned, I was sent for by T.T.K. who asked me how I could agree to join the Prime Minister's office when he had always assumed that I would return to him if I returned to the Government. I was taken aback. The question of my joining the PM's office had not arisen. I was not asked and I would

not agree, even if asked. I had indeed promised T.T.K. that I would return to the Ministry of Finance, if I returned to the Government at all. The least I could do to repay his kindness was to consult him before considering any change in this position; and, in any case, no one had approached me. T.T.K. said, when I apprised him of the position, that L.K. must be up to some mischief as he had joined the PM's office as Secretary! I got in touch with L.K. who simply said I was indeed joining the PM's office, that all was settled, and the PM had agreed. I had to tell him that he was mistaken, that I would return to the Ministry of Finance, if I returned to the Government at all. And so I did, on 1 January 1965. I had enjoyed my year at the Delhi School, particularly the teaching; and even today, I meet people who remind me that they were 'my students'. There is no satisfaction greater than the affection of those one has taught, however briefly. But I had also acquired a taste for being in the thick of things; and the Ministry of Finance was my natural home.

*Shastriji**

By then it was already clear that Shastriji had a mind of his own, that he was shrewd, had an iron will, a clear view of where the country should be going, particularly in economic policy, and a personal style which was decisive as well as participatory and indeed conciliatory. I witnessed his shrewdness and caution first-hand on several occasions. He had agreed with L.K. that I should be asked to join his office. Nevertheless, he made further enquiries and asked L.K. a few days later whether he had approached me. He made no secret of the fact that in the meanwhile, he had consulted others. On another occasion when I had to obtain his clearance on an important file, he asked me to see him in person with the file. He did not want me to state my case; he wanted instead that I should read out my file note slowly to him. That way, he said, he understood better—a modest touch to a simple man! From

*London, 16 May 2000.

time to time, he asked me to explain what I had just read out. At the end, he said it made sense and we should go ahead. But he did not sign the file. He asked me to leave it behind. It was only after consulting some others that he sent it back with his signature.

His clarity of purpose and iron will were clearly demonstrated in the 1965 Pakistan war. But his views on economic policy have not received enough attention. He was too shrewd to give an impression that he was out to undo the work of Panditji. But I have no doubt that that is precisely what he would have done if he had lived longer. Already, he had said enough about giving greater importance to agriculture. In the Gandhian tradition, he disliked controls and the corruption they bred. He was not at ease in the company of big industrialists, and his sympathy for the common man made him more willing to give priority to consumer goods industries. At the same time, he was no ideological visionary and understood the connection between defence and modern industry. And as was soon to be seen, his stand on the Bank's advice on many occasions would put him in the front rank of modern reformers. I have no doubt his untimely death changed our recent economic history and delayed economic reform by some two decades.

Shastriji's thinking was anathema to T.T.K. and there grew between them much hostility—real and outspoken on one side, and real and unspoken on the other. For T.T.K., none was good enough to succeed Nehru and certainly not the diminutive Shastri who would not pay homage to the master at every turn. T.T.K. used to drop into my office almost every day fulminating against Shastriji and asking me to draft a sharp letter of resignation. I would draft one, he would correct it and I would draft another and when he finally approved it, I would tear it up. He would laugh and go away. And the game would resume a few days later. I wish I had encouraged him to send one—that would have been better than being eased out, as he was ultimately. A matter of great sadness and humiliation for T.T.K. even if he described it as a relief, and another example of Shastriji's boldness.

My own life in the Ministry on my return was also rather different from that before 1964. V.K. Ramaswami had joined the

Ministry as Chief Economic Adviser when I went to the Delhi School. On my return, he very nobly decided to stay on as Economic Adviser rather than return to the Commerce Ministry. He liked the work in the Ministry of Finance and had already made himself indispensable. His analytical bent and contacts with academic persons in India and abroad were an added asset. He was a loyal and lovable colleague and soon became almost a family member. I was now spending most of my time abroad on 'economic diplomacy' rather than at home on economic policy. By now, I had also shed the Planning Commission responsibility. Manu Shroff added ample strength on both the domestic and the foreign front. Bhoothalingam as Secretary ran his very able team well as a coherent and friendly group, and was himself no mean economist. By now, I had also gained sufficient acceptability in all echelons of the Civil Service.[10] What this meant was that with T.T.K.'s blessings, I was essentially doing 'special jobs' rather than running the Economic Division which by then had become quite self-reliant.

Managing Agencies and Monopolies

One special job was the chairmanship of the Managing Agency Committee. It was just like T.T.K. to ask me to chair the Committee and then include in it as members, colleagues senior to me, like B.N. Adarkar. But my seniors showed no resentment and we worked well together. We were asked to examine whether the Managing Agency System should be continued in the established industries. The Committee's recommendations were cautious. But in the event, the Managing Agency System was abolished. If my memory serves me right, P.S. Loknathan had written a book on it which we read during our undergraduate days and all nationalist opinion was against the system. It was felt to be a nefarious device of the British whereby a few British managers could control vast industrial, commercial and financial companies in India without any significant financial stake. In so far as a single Managing Agency managed many firms linked with each other in some way or another, there was danger of monopolistic or manipulative action

based on insider information. The system also denied the shareholders any say in running the companies they owned.

Looking back, I wonder whether the Managing Agency System, despite all its drawbacks, did not serve some useful purpose. If management talent is scarce, if family businesses are inefficient or suspect or becoming difficult to manage as they become sooner or later, if professional managers are needed and trained, what is wrong if a form of management is devised which brings a group of managers together as a firm? I suppose the Managing Agency System was dying any way. It was not much in demand. And so it disappeared, not with a bang, but with a whimper. But the question still remains: can something like the Managing Agency System return?

It was during 1965, I think, that I served as a member of the Commission on Monopolies and Restrictive Practices. The guiding spirit in that Commission was R.C. Dutt, a senior ICS officer committed to leftist causes. Even the Mecca of capitalism, the USA, believes in control of monopolies and restrictive policies. This makes sense as competition spurs efficiency only if it is open and free and widespread. When monopoly is inevitable, regulation is called for. As a member, I could only take part in the discussion of major issues—I had too much on my plate to pore over drafting details. While much in the Report was commonplace, Indian leftists have made their own contribution to economic literature in the shape of 'Concentration of Economic Power'. This has nothing to do with the quality of competition in markets. It is a 'power' concept, that is, a concept which seeks to control the so-called economic power that any business group can enjoy through the totality of business ownership or assets. Thus the Tata group cannot have assets above a certain financial limit. Apart from the vagueness of the concept of a 'group', such a limit has no economic rationale and can at best be justified in political terms. I opposed this idea to no avail. The idea that I did not advocate then—but would do so now—is that the term 'restrictive practices' must apply to all restrictive policies, whether of management or of labour. In India, much of our inefficiency, indiscipline and lack of competition is the result of allowing labour to usurp the powers of management

and to enforce restrictive work practices in the interest of those already employed and to the detriment of everyone else, including industry, consumers and the large body of unorganized and unemployed labour. One would wish to see 'restrictive practices' by the government banned as well.

An Interlude

In the summer of 1965, I spent a very pleasant month in Cambridge at the invitation of the British Council. This time, I stayed at my old college as a visitor and occupied a grand suite of rooms in Gibbs Court. It was wonderful to have all the time at your command in beautiful surroundings, and I used it to write a paper for a conference in Washington D.C.[11]

It was at that conference that a Russian delegate asked me why I thought that a country like the Soviet Union had an obligation to assist India. I was at a loss what to say and replied tongue-in-cheek that I was the only Hindu in the room and believed in life after death. Since this can neither be proved nor disproved, the probability of life after death can be taken as one in two. Since two-thirds of the world was poor, there was one in three chances that my Russian friend might be born in his next life in Zambia or India. Does it not make sense for him to ensure his future by doing something in this life which might make Zambia or India better places to live in after, say, thirty or forty years? Everyone laughed. But I was told many years later that I had in fact anticipated John Rawls's argument for altruism. If we looked at things from the point of view of an unborn child which is in complete uncertainty about what kind of family he or she might be born in, it would make sense to say that extra money should go to the poor rather than the rich. That would make his or her lot a lot better if he is born in poor circumstances and not all that bad if he was born with a silver spoon in his mouth. This I think is as good an argument as any for a more equitable distribution of income. Who can be most completely objective and uncertain of the future as an unborn child—or someone who is transiting from this life to another?

Devaluation and the World Bank

Externally, much had changed since 1963. In the World Bank, the civilized and urbane southern gentleman with *gravitas*, Eugene Black, had been replaced by a New York banker of no great pedigree, George Woods. There was a peculiar psychological problem in his relations with India. As a banker, he was employed by the Government of India as a consultant and financial adviser, and I had seen him being deferential to T.T.K. Now he was a big boss in his own right, and the chemistry between him and T.T.K. was just not right. George Woods was also perhaps a little manipulative by nature: instead of straight but friendly talk, he seemed to relish strategies, more like a chess player than an ally; and he seemed to have made up his mind who needed to be checkmated. T.T.K., on his part, was at his acerbic best in referring to Woods.

The first visit of Woods (and his wife) to India as President of the World Bank was almost a disaster. My own experience of George Woods is that he had a charm of his own, could be ingratiating and was very able. But there was something not quite cricket about him.

In fairness to Woods, it must be said that all he was trying to do was to make India change certain policies and to link Bank and Consortium support to the pace of these changes. Most of the changes such as import liberalization, rationalization of export subsidies, some decontrol and delicensing, and greater attention to food production were badly needed and had support in India. The Americans and others were insisting on the same. Lyndon Johnson in fact had pursued a 'ship to mouth' policy of food aid to compel India to introduce far-reaching reforms in the agricultural sector. The problem was the more or less open advocacy of devaluation by the Bank. More than the merit of the case, the issue was style or the manner of advocacy. After all, there was much support for devaluation in India in academic as well as governmental circles. Politicians and Finance Ministers are never in favour of devaluation as it sounds like an admission of defeat. Also, talk of devaluation itself creates a crisis, making their task

difficult. There was legitimate anger, therefore, that instead of the issue being discussed at some level and in great secrecy, the Bank itself was seemingly trying to create support in India for the idea by open advocacy. The fact that the exchange rate is an IMF subject on which the Bank was making all the noise was also an irritant. But in those days, the Bank took special delight in sidelining or humiliating the Fund which had then a mild and very civilized Frenchman, Pierre Paul Schweitzer, as Managing Director. George Woods had attracted Irving Friedman, an ambitious and able American head of the Exchange Restrictions Department in the Fund to the Bank as his personal adviser; and Irving—a very good friend of mine—was not above trying to run the Fund from the Bank. In this, he had other supporters in the Bank.

For quite some time, devaluation was in the air and the subject of light-hearted banter. At one meeting when a Bank mission called on Bhoothalingam, there was some persistent questioning by a Bank official of the target of production for steel—some six million tonnes, I think. At one point, Bhoothalingam, exasperated by the persistence of the questions, remarked, 'My dear fellow, I can guarantee that we will reach the target of six million tonnes even if we have to devalue the tonne.' I myself had a less than happy experience at one of the meetings of the Aid India Consortium in Paris. Simultaneously, there was taking place a meeting in Paris under the auspices of the OECD where a number of my friends from the UK and the USA were participating. I had agreed to join them over dinner after our meeting. On reaching there, I was asked how the Consortium meeting went, and without thinking I said, 'Not bad, we were lectured at for eight hours and we got a billion dollars. Not a bad rate of exchange.' One American present there, Hollis Chenery, reported back to his Government that, unlike Pakistanis, the Indians were arrogant and did not want to listen to good advice! This, of course, went down as a bad mark against me as well as against India; and on my return to India, Bernie Zagorin, the chief US Aid officer in New Delhi who knew me well, said, 'I.G., why can't you keep your big mouth shut? Don't you know that most American academics have not gone to Cambridge and developed your sense of humour?'

The crunch came with the Bell Mission. Bernard Bell had made a reputation in Indonesia where he had successfully pioneered widespread economic reforms. His credentials as an economist were good. If I remember right, the Bell Mission was a massive affair with the whole gamut of the Indian economy as its scope and a number of expert teams to focus on different sectors of the economy. Most of these teams worked very well with Indian officials and the interaction was cordial and beneficial. The trouble came with Bell's own area of choice—the external sector—and his open advocacy of devaluation. In later years, he made a serious effort to show that he was a friend of India and of Indians and I think we judged him too harshly at the time. Partly, we were used to Bank teams led by Englishmen who spoke our language and found the new Woods era with its preponderance of American accent and style somewhat off-putting. But in part, Bell's own personality was to blame. He was at the time at the top of his professional curve which bred some arrogance; he seemed impatient to achieve results in India as a crowning seal of his arrival; and his boss in Washington was not inclined to guide him in diplomacy. What could have been a civilized dialogue somehow turned into a slanging match. The pity and the irony is that most of us involved in the dialogue were convinced of the wisdom of much of Bell's advice. What we needed was discretion and patience till we could prepare the ground at home—which was not easy with T.T.K., but not impossible with Shastriji. I knew that Bhoothalingam as Economic Secretary, L.K. Jha as PM's Secretary and P.C. Bhattacharya as RBI Governor—not to mention the economists in the Ministry—were all convinced that devaluation was necessary and unavoidable. Our exchange system had become such a maze of multiple exchange rates that no one knew what the actual average operating rate was. The distortions, inefficiency and the corruption bred by a system of rampant and almost riotous multiple exchange rates were there for all to see. Apart from anything else, the economic case for introducing a single rate of exchange—with only minor departures—was overwhelming and such an exchange rate obviously had to imply a formal devaluation. Its magnitude

was a different matter and could not be discussed without a decision first, in principle to change the official rate. My own position was a bit awkward. I was certainly in favour of devaluation. But I never said so publicly which made some of my colleagues think that I was a part of the obstacle. I knew too much of what was going on to feel free to air my views; and as long as the government was not ready for a change, we had to defend our policies. There was also the T.T.K. factor: one did not want to infuriate him by rumours he was already counting villains in his team. I perhaps had also the illusion that some of us could be the ultimate bridge to approach him.

I remember one stormy meeting in the RBI Governor's flat in New Delhi when Bhattacharya and I met Bell by himself. He first expanded his ideas to us. All of us had too much to drink and little to eat. Bhattacharya thought he could charm Bell into accepting some kind of a fig leaf or a first step: anything to soften the blow. The alternative of uniform taxes on imports and subsidies to exports was something we had toyed with—although this would leave a wide open loophole for invisibles. But Bell was adamant—and even offensive. The meeting did not end on a pleasant note. But as soon as Bell had left, both of us asked ourselves: why are we interested in a charade? What came in the way of an honest amputation except personal or political pique? The two of us at least knew where we stood.

It would be idle to pretend that all this debate was about economics only.* Money was also very much at the centre. Bell made it abundantly clear that the availability of Consortium aid depended on our accepting his advice and that in this, he was speaking not only on behalf of the Bank, but the US and other members of the Consortium as well. The corollary also was that acceptance of the advice would yield rich dividends, especially in the form of non-project aid to support import liberalization. The significance of this point was not lost on us, particularly not on Bhattacharya

*London, 17 May 2000.

who was not an economist but was an eminently sensible and practical person and had the main responsibility for managing foreign exchange.

Against this background, the forthcoming Bank-Fund meeting in Washington in the autumn of 1965 was obviously very important as it provided an opportunity for future discussions with top management in the two institutions. Surprisingly, I have little recollection of this meeting. I am not sure if T.T.K. went to Washington. What I remember is that I was asked to stay behind in Washington and have some low-level discussions with the Fund staff, presumably in preparation for some formal Fund consultations. The strategy was to shift the focus from the Bank to the Fund and to test the waters in the Fund. We had made it clear to the Bank that the exchange rate was none of their business, that it was something between us and the Fund. In any case, with the talk of devaluation, our foreign exchange situation had also to contend with possible speculative outflows on top of the general weakness. Preparing ground for a Fund drawing was imperative.

It was as I was about to return to India that I received news of the Pakistan attack on Kashmir. I remember M.G. Kaul who was also there at the time and was familiar with defence matters assuring me that we were well prepared for the eventuality. But the initial news was very disconcerting. There were exaggerated reports in American newspapers about the superiority of Pakistan army and its US supplied equipment and some undisguised glee at our discomfiture. The contrast from China in 1962 to Pakistan in 1965 was striking. The British attitude under Wilson was even more openly pro-Pakistan. Such were the vagaries of the Cold War.

We returned to Delhi immediately. For the first time in our life, my wife came to the airport to receive me and to reassure me that everything was fine: we had counter-attacked and were winning, that the country had responded manfully and that everyone was disciplined as could be seen from the blackout in Delhi. She was at her patriotic best; and subsequent events justified her.

Shastriji's courage in crossing the border and carrying the battle to the enemy's own frontyard was a big gamble and it was that which rankled with the US and the UK. But it paid off and cemented Shastriji's hold over the leadership of India. Little did we know that one fall-out of this success and boldness was similar courage on the economic front. It was towards the end of December that T.T.K. was relieved and replaced by Sachin Chaudhuri, a prominent lawyer from Calcutta whom very few people outside Calcutta knew. He was neither a politician nor an expert in economics or business. At first, we thought it must be Sachin Chaudhuri of the *Economic Weekly*—which would have been equally astonishing. And we could not imagine what the distinguished lawyer from Calcutta would bring to the Ministry.

It was soon to be clear that L.K. and Bhattacharya had convinced Shastriji that T.T.K. had to be replaced—a suggestion which would not have been unwelcome to the PM in any case. The war had made it even more urgent to come to terms with the Bank and the Fund; and this was not possible with T.T.K. around. The choice of Sachin Chaudhuri was strange, but clever. As a political lightweight, economic illiterate, a thoroughly pleasant and agreeable professional with impeccable manners, he would be pliable and do what he was told, by the PM and by his advisers. To add to all this, he was a personal friend of Bhattacharya so that he would be pliable not just to the PM but to the RBI Governor as well. And he could, of course, conduct himself with grace and humour in international negotiations. In all this, Sachin Chaudhuri fulfilled all expectations, and more. He left behind an impression of a very warm and decent minister who, as he himself put it, left by the front door in 1967 when he was defeated in his first and last Parliamentary election. But in the short period that he was in the North Block, he left his mark on Indian economic history.

Within days of his joining the Ministry, I was asked to join Bhattacharya on a visit to Washington. I was given hardly a day to get ready. I was to catch an Air India flight from Delhi and Bhattacharya was to join the same flight from Bombay. A few hours before I left Delhi, Chaudhuri himself handed over to me a small envelope when no one else was present. If I remember right, I was sitting in my car on the North Block ramp and he drove up

to me to give the 'brief' which I was to hand over to Bhattacharya on the plane in Bombay. I was not told what the 'brief' contained or what our Mission was about. I learnt about it from Bhattacharya on the plane.

The 'brief' in fact was a letter from the FM to our Executive Director in the Fund, J.J. Anjaria, authorizing him to inform the Managing Director of the Fund that the Government of India was prepared to devalue the Indian rupee in due course after discussions about possible Fund assistance and about the extent of devaluation. It was assumed that the Fund and the Bank would cooperate and a package of Fund drawing and Bank non-project assistance could be worked out to coincide with the devaluation. Further Consortium aid would follow. Given the fact that we had just emerged from a war and had agreed to a cease-fire, no one expected prompt action on the exchange rate front. And we wanted to stage everything carefully. I believe I stayed behind for some detailed discussions with the Fund staff. Thus the deed was done in Shastriji's life and with his full knowledge and support. I have no doubt that if he had lived longer, devaluation would have come earlier, and been managed more smoothly, accompanied or followed by far-reaching reforms. It would also have been politically less divisive given his enormous prestige after the victory in the Pakistan War.

But it was not to be. Shastriji was taken away from us in Tashkent. With a new and less confident, and indeed less predictable government, everything had to start all over again—and with India not batting after winning the toss, so to speak.

The Baptism of Indira Gandhi

After a short interregnum, Indira Gandhi was installed as India's Prime Minister early in 1966. The caucus that made it possible hoped to rule from behind the throne. In the early days, there was much reason to believe in the tale of the *Gungi Gudia*, or 'dumb doll'. Mrs Gandhi spoke little in those days and no one knew what went on in her mind. Obviously, much did. But she kept her counsel much to herself.

She had served as Minister of Information and Broadcasting in Shastriji's cabinet. But she had kept a low profile. Soon after taking charge, she had called a meeting of the so-called 'intellectuals' in which I was, for some reason, included. The idea was to get advice from the good and the great. Much was said by those present. When my turn came, I simply said I had nothing to say as I knew nothing of Information and Broadcasting. She laughed and said rather sarcastically: 'Obviously you and I are the only ones who do not know anything about I&B'. There was always this 'love and hate' or 'pull and push' between her and experts or persons supposed to be more knowledgeable. She wanted to be known that she liked them; but she did not quite trust them. She was more at home with creative persons like writers, artists and craftsmen, and made it a point to meet them whenever she could.

Soon after she assumed charge as Prime Minister, President Lyndon Johnson, who had invited Shastriji to come to Washington as his guest, wrote to her to keep the date: 'I had invited the Prime Minister of India and he had agreed. So you have to keep the date.' The invitation was timely, as there was much to be said for establishing a new understanding with the new PM and Washington, including the financial institutions located there. Her advisers, I am sure, were keen on her going; and rather reluctantly, she agreed. She asked me to accompany her. At first, I had to plead inability as we were expecting our first child then and that there had earlier been problems on that score. But Rehana obliged and arrived a few days before Mrs Gandhi's departure; and I had no choice but to be a member of her party.

The party from Delhi included L.K. Jha, Pitambar Pant, myself and Mrs Gandhi's personal staff. B.K. Nehru was already in Washington as ambassador. In London, we changed planes and boarded the presidential plane sent for Mrs Gandhi. Among those who joined us there were her two boys—Rajiv and Sanjay—and someone mysterious at the time, P.N. Haksar. Most of us did not know him and had no idea why he was there. It soon was to be clear that he was to succeed L.K. whom Mrs Gandhi did not trust. Haksar, a very able foreign service officer, was apparently an old

friend and a leftist who was closer to Mrs Gandhi personally, if not ideologically. There was nothing basically ideological about Mrs Gandhi. Everything was as it suited her at the time. Haksar had another leftist friend in the London High Commission, A. Bakshi of the Audits and Accounts service. He too was to play a part in L.K.'s life—and mine.

In many ways, the visit was a one-sided affair. Everyone knew that Mrs Gandhi could not be rushed; that behind her docile façade, she was the imperious daughter of a proud father, she had to be humoured rather than lectured to. Even George Woods could not think of checkmating her; and the old fox Johnson was chivalrous. Everybody said what they wanted to 'in India's interest'. Johnson spoke about food and agriculture in the main and the rest about the rest. Mrs Gandhi listened politely, even regally. There was no question of making a response. No commitments were expected or made. In many ways, it was like a royal visit.

For me personally, it was a happy interlude. I had no speeches to write or briefs to prepare. Pitambar and I were not senior enough to attend most meetings. I could relax with my friends. In New York, we even celebrated Rehana's arrival with champagne and a visit to a disco where we were not charged as we were part of Mrs Gandhi's party! I had a difficult time trying to abscond for a while to buy a present for Rehana. What I bought in a hurry and almost surreptitiously at the last moment—a plastic kite in the shape of a bird—could be folded but the wooden spine was too big for my suitcase so that I had to carry it in my hand, causing many comments and some embarrassment.

On the return journey, we were ferried in the presidential jet to London from where a Russian plane was to take us to Moscow. Prime Minister Wilson was most anxious to atone for his faux pas in the Pakistan war and invited Mrs Gandhi to spend a day or two in London. But Mrs Gandhi would have none of it, and Wilson had to be content with calling on Mrs Gandhi at an airport hotel and giving her lunch there. For the most part, Mrs Gandhi listened again and confronted Wilson with her Mona Lisa smile.

The halt in Moscow was just for one night and by then only Pitambar and I were left in Mrs Gandhi's party. But the visit was

truly memorable. Prime Minister Kosygin received Mrs Gandhi warmly. Our ambassador, T.N. Kaul, read out the usual list of projects we wanted Soviets to implement for us, including more machine-building plants. Kosygin explained patiently that he was a professional engineer which Kaul was not and that we did not need any more machine-building plants. What the Soviets had already supplied was enough for us for many years to come and all we needed was to use well what we already had. In that, the Soviets would provide all training and other facilities. He made it clear that he was not trying to save on Soviet resources. He was more concerned with the waste of Indian resources. Kaul certainly was not convinced. But I have no doubt that Kosygin spoke as a true friend of India and as a professional. The Soviets are too often blamed for selling us a wrong model of development or a lot of useless equipment. I am afraid the blame is at least as much on our side. They did not sell us anything as a price of their friendship. We extracted it from them and we drew our own right or wrong lessons from the Soviet experience. The blame for inefficient use of equipment must also lie at our door. Soviet equipment may not have been the best in the world. But it was good enough—and we got it on very concessional terms.

The spirit of the visit was best exemplified as Kosygin was taking leave of Mrs Gandhi. He put his hand on her shoulder and said that he was old enough to give her some advice. He said: 'Madam Prime Minister, I know how difficult the role of a Prime Minister is; and yours is perhaps the most difficult of all. Do not neglect your health and do relax from time to time. It is necessary for your work. If you cannot get away from work in India, you come to our country even if it is for two or three days. We will leave you entirely free to rest and recuperate.' This was said with the utmost affection and sincerity.

There was also an amusing side to the visit. On arrival, Sketchkov—the Russian minister in charge of economic relations with India—who was to escort me, was puzzled by my kite and asked me if I was carrying Mrs Gandhi's personal flag or insignia. After the banquet and Kosygin's departure, Pitambar and I had to

leave Mrs Gandhi's dacha as we were to stay in a hotel in the city. We had to pass through the kitchen and the palatial dining hall, where we found the staff occupying the seats we had occupied a couple of hours earlier and having great fun eating and drinking. They were not at all fazed by our appearance and quietly ushered us out. Call it the spirit of socialist equality or an example of socialist spoils and sleaze. But it was a sight to remember. In the hotel, the old woman attendant kept walking into the room at night from time to time to check what I know not. And the next morning, my request for orange juice created a commotion—what seemed like hours later and a lot of flurry, someone came and said they had no orange juice but had brought some caviar instead! Who says you cannot eat cakes if you do not have bread?

Devaluation and After

On return to Delhi, one had to come down to earth. Mrs Gandhi had to make up her mind on devaluation. She did not lose much time on it, but took good care to consult a large number of persons. I know that Jagdish Bhagwati and K.N. Raj were consulted. I myself took the veteran Professor Gadgil to see her and he corroborated our own advice. She had now a new team of so-called professionals with whom she was more at ease. C. Subramanian as Agriculture Minister was all sold on Bank advice, and not just on agriculture. Ashok Mehta as Planning Minister was atoning for his socialist past and was most enamoured of his new-found faith in economic liberalism. Some of us were doing our usual job—talking and briefing quietly behind the scene. Mrs Gandhi too, it must be said, was very modern in her outlook and felt no filial duty to follow in the footsteps of the father, internally if not externally. If any contrary advice was given to her, I am not aware of it. Many persons who claimed later to have opposed the idea were either not consulted or were economical with truth. We all had made it clear that devaluation had to be combined with other things to yield results, like much stricter fiscal discipline, import liberalization and generous project and non-project aid which we had

good reasons to think would follow. But advice for outright rejection was in large part an afterthought.

Once the mind was made up, we had to act swiftly. A team led by Ashok Mehta—with Govindan Nair, V.K. Ramaswami and K.S. Krishanaswami to assist him, went to Washington to discuss with the Fund the question of the level of the new rate and related questions. Manu Shroff joined them when the discussions had progressed to the point of deciding on figures. There was general agreement that if we had to bite the bullet, we might as well take a big bite as one does not devalue every day. About the only worry was on the score of the budgetary impact. Our calculations showed that at worst it would be neutral. No one expected a dramatic improvement in the balance of payments in the short run, except for a reversal of capital outflow. Hence the insistence on more aid as a prerequisite. In the long run, however, devaluation would help increase or at least maintain our share in world trade. We were aware also that part of the devaluation in monetary terms would be offset by price rises so that real devaluation would be more modest. Altogether, a new rate of Rs 7.50 per US dollar—a devaluation of more than 50 per cent—was considered suitable. This was more than what the doctor (the IMF) had ordered!

The paramount consideration was maintaining secrecy in the closing stages. And it must be said that when it came on June 6, it took people by surprise. We all had had to work hard to preserve secrecy. But there were anxious moments. On the crucial day before the Fund Board meeting, L.K. Jha and I had to attend a dinner given by the Cabinet Secretary, Dharam Vira. It was in honour of a visiting American military team and it was agreed that L.K. and I would accept the invitation to avoid suspicion whereas Bhoothalingam would not, to take care of things. During the dinner, L.K. and I were called out twice to receive some message from Bhoothalingam. At night, my wife confronted me and asked me what was so important which took L.K. and me out at the same time and asked: 'Are you devaluing?' I said no as casually as I could and explained that it was about some Chinese military movements. She, of course, was prompt in retorting why I was more

needed on military matters than the Cabinet Secretary; I had to play on her reaction to Dharma Vira's speech at the dinner which she had not liked and mutter that no one took him seriously. She knew that L.K. always liked to use me as a sounding board. I am not sure she was convinced. But she fell asleep anyway.

The Cabinet meeting had to coincide with the Fund Board meeting and the announcement had to be made the same evening. At the Cabinet, Manubhai Shah, the Commerce Minister, opposed the move as all of his prerogatives of creating new multiple exchange rates were to be taken away—at least temporarily as it happened. But for the rest, it was a short and smooth affair. Anjaria was to inform us as soon as the Board decision was taken and we had taken care to keep the lines clear to the telephone in Bhoothalingam's room. Ramaswami and I were waiting in the room (the others had gone home) and we heard Anjaria's voice, but he could not hear us and kept asking whether we had got the coded message about the Board's approval. After a while we had to end the conversation without worrying about Anjaria as what mattered was that we had heard—and we had to rush to the Finance Minister who by design was dining with some friends and to tell him that he could now leave and go to the All India Radio and read out the speech which was in his pocket.

Almost simultaneously with the radio announcement, all Chief Ministers were handed over a note explaining the rationale of the decision. This remarkable action reflected the tradition set by Panditji to take the states into confidence on all important matters. We had sent that morning a bunch of officers, some on special planes, to different state capitals with the note. It was a job to explain what was so urgent and secret that it took such elaborate transmission arrangements. And Manu Shroff found the perfect alibi: we had decided to stop all overdraft facilities to all the states to improve the financial situation and to inculcate some discipline in them. No one smelt a rat.

P.N. Dhar and I were asked to visit some state capitals and meet state cabinets to explain things and answer queries. The results were almost ludicrous. Dhar Saheb and I flew to Lucknow where Suchetaji[12] was to have a Cabinet meeting. We were waiting on the sidelines. Everybody was busy with the sweets and savouries served and no one had any question to ask! My visit to Bangalore was even better. I was well received and had an excellent South Indian lunch on a banana leaf in a traditional and very popular restaurant. But I was told the Assembly was not in session, and I could not see anyone. I was supposed to talk to some Assembly members as well as ministers. The truth of the matter is that devaluation was neither a political nor a popular issue, especially for the states. It had resonance in business and academics, but not much elsewhere. What made devaluation a matter of great debate and controversy was the fact that for a variety of reasons it did not succeed as expected and was followed by a period of profound economic hardship.

This hardship had little to do with devaluation. It was largely the product of food shortages, successive bad monsoons and the accumulated impact of bad policies, including progressive fiscal improvidence. Admittedly, there was great anger at the fact that the Consortium meeting that followed the devaluation was a big disappointment and indeed a betrayal. The much advertised non-project assistance of a billion dollars did not materialize and there was the usual wrangling about projects and denial by delaying. The hoped-for liberalization of imports could not be attempted, with the result that there was no spurt in growth from greater utilization of capacity. The Fourth Plan which should have begun in 1966 had to be abandoned and we had a plan holiday for three years (1966–7, 1967–8 and 1968–9) when we had only annual plans. The Fourth Plan period began not in 1966 but in 1969. President Johnson's 'ship to mouth' policy on food aid created considerable resentment. All this created a climate of despair and for Mrs Gandhi, her first test of popular disenchantment. It was in this climate that the 1967 election had to be fought, and the smouldering divisions in the Congress and the ongoing silent war of succession made things look particularly bleak for Mrs Gandhi and the country.

Endnotes

1. I had told Anjaria, in response to his offer, that I would be 'more than happy' to accept a salary of Rs 1500 per month. Despite his best efforts, I was given Rs1480 and not Rs 1540 per month as there was no step of Rs 1500. It was argued that in view of what I had said, audit would object if I was given a salary higher than Rs 1500!
2. It took more than four years before I was given the status and salary of an Additional Secretary which Anjaria had enjoyed as Chief Economic Adviser.
3. If I remember right, the QLI was developed by the Yale University and was quoted regularly by US Development Agencies.
4. I have inserted this rather analytical and controversial section as the subject-matter is important and one which has often perplexed me—and the perplexity continues as would be evident, I hope, from the qualified nature of most of my observations. If it provokes some discussion, my purpose would be served.
5. Obviously, the case of wholesale expropriation of private property is a different one. Mere nationalization will not do: it has to be combined with inadequate compensation. But even then, the worm of efficiency will turn: unless public assets are efficiently managed, the rate of growth will decline and the State will have the honour of presiding over a diminishing empire.
6. Even here, while each country benefits, there are losers and gainers in each country and it is the dynamics of the struggle between the losers and the winners which determines how free such trade would be in real life.
7. The formulation that devaluation would shift consumption, production, exports and investment away from forms with higher import content and towards those with higher domestic resource component is free from this criticism.
8. It is sometimes argued that pronounced changes in relative prices can be prevented from leading to a general rise in prices by a tight rein over the growth of monetary demand. But this is easier said than done—and if done ruthlessly, can create a serious stabilization crisis or recession.
9. The supplement to the Economic Survey issued in July 1966 soon after the devaluation argued that this step was 'calculated to correct the adverse effects of inflation on the country's balance of payments'.
10. Early in 1966, I was finally given the scale and pay of an additional secretary.

11. 'Foreign Capital and Domestic Planning' by I.G. Patel, published in *Capital Movements and Economic Development*, proceedings of a conference held by International Economic Association, edited by John H. Alder and Paul W. Kuznets, Macmillan, London, 1967.
12. Sucheta Kripalani was the Chief Minister of Uttar Pradesh then.

5

The Rise of Mrs Gandhi 1967–72

It was clear to those of us who were in the thick of things that the difficult economic situation could not be tackled without a strong and united government.* The results of the 1967 elections were thus crucial. Another leadership struggle was inevitable given the fact that the first year of Mrs Gandhi's rule was not a shining success; and the chances of infighting would be greater if the Party fared badly at the elections. But whoever won, it would be better if there was rapprochement and willingness to work together.

The 1967 Election

Pitambar Pant, P.N. Dhar and I got together and decided that we could not just stand by without doing something. It was agreed that Pitambar and Dhar Saheb would call on Mrs Gandhi and I would approach Morarjibhai who was then Chairman of the Administrative Reforms Commission. Our mission was to persuade our respective quarry that whoever won the leadership race should invite the other to join the Cabinet in an important position, present a united front and work together. The situation was very critical and demanded nothing less. In a way, we were rather cheeky.

*London, 18 May 2000.

Imagine telling Mrs Gandhi or Morarji what to do if she or he did not win—because the loser too had to cooperate just as much as the winner had to be magnanimous. But we did; and the immediate results at least were as we had wanted them.

I was nervous about calling on Morarji. Ultimately, I decided to hide behind my daughter, Rehana. Morarjibhai had come to the hospital to visit my wife when the baby was born. In Gujarat, we call on our elders on New Year's Day and seek their blessings. As that day fell during the election period, I decided to take Rehana to Morarjibhai's place early that morning. The house was full. Morarji was happy to see Rehana. After some time, I had to draw him into another room to tell my tale. His response, which came after some thought, was: 'Did you say, some of you think this way, or is this your own idea? Have the others seen Mrs Gandhi?' I assured him that I represented the views of many persons and that Pitambar and Dhar Saheb would call on Mrs Gandhi if they had not already done so. Our meeting ended cordially although he gave no inkling of his reaction.

Eventually, Mrs Gandhi returned as PM and Morarji became the Deputy Prime Minister in charge of Finance. Although this arrangement lasted only some two years, I think much was quietly achieved in that time. Morarji pursuaded Mrs Gandhi to invite the much respected Gadgil to be the Deputy Chairman of the Planning Commission and assured Gadgil that he would have full support of the Finance Ministry. Contrary to the belief in some quarters, Gadgil was Morarji's choice and not Mrs Gandhi's and the two men had great mutual respect. It needed someone of the stature of Gadgil to tone down the planning fever and recommend a plan holiday till the economy had caught its breath. In the Finance Ministry, we were slowly rebuilding our bridges with the outside world and putting the financial house in order. C. Subramaniam in the Ministry of Agriculture showed great courage and administrative skill in ushering in an altogether new agricultural order which led to the Green Revolution. In our small way, we in the Ministry of Finance supported Kurien[1] in getting vast quantities of milk powder under aid—a step which ultimately opened

the way to the White Revolution. A similar revolution was under way in regard to fruits and potatoes. We succeeded in getting more non-project aid and financing of some local expenditure by aid which gave a new impetus to industrial production.

Morarji's 1967 budget had a unique feature: it was the first and the last budget in which there was to be no deficit financing in the sense in which we used the term then, that is, no borrowing from the RBI for meeting budgetary outlays. We had always justified some deficit financing on the ground that a growing economy which was also becoming more marketized needed a growing money supply. It was for the first time in a budget speech that we confronted the question as to why this legitimate scope for money creation should be appropriated entirely by the public sector. After all, the demand for money arose largely in the private sector where the bulk of economic transactions took place. Why should the RBI not finance commercial banks rather than the Government to achieve the desired increase in money supply? There was also the consideration that the much needed increase in foreign exchange holdings of the RBI would in any case add to money supply. A conscious decision was taken to have no deficit financing for the Government. This was a reflection of the spirit in which the new Government was to address its tasks. Alas, in the event, there was a deficit. But the intentions were sound.

It was around that time that Khruschev visited India. He thought deficit financing was wrong and unnatural and I was asked to see him and explain to him why sometimes it was necessary. The meeting did not materialize. But here is one more example of how Soviet communism often saw eye to eye with Washington capitalism.

Mrs Gandhi's election victory in 1967 was not spectacular; and she was suspicious that foreign, that is, CIA money had been used to support her opponents. In fact, she was suspicious of Indian academics and intellectuals who visited foreign countries, particularly the US. She felt they were brainwashed during such jaunts. The result was the imposition of rules whereby no one in any government-aided institution could travel abroad or invite a

foreign academic without prior government approval. I remember Mrs Gandhi losing her temper when at the Cabinet meeting I had cautioned that this would lead to inordinate bureaucratic delays and annoyance. She said she knew what my academic friends were upto—even if I did not!

Economic Secretary

I have no recollection of the 1967 Consortium meeting. What I do remember is the 1967 Bank-Fund annual meeting which took place in Rio in Brazil. It was a relaxed affair with no great issues to settle or deals to be struck as far as we were concerned, although it was at this meeting that it was decided that the Fund should examine ways of creating international reserves in ways other than increase in quotas. My memory primarily is about my own illness. I developed a severe cold and slight fever in Venezuela where we had been on a State visit for a few days. By the time we boarded the plane for Rio at Caracas, I had high fever. To add to the trouble, there was utter confusion about air bookings. Apparently, everyone was going to Rio, and everyone was a VIP with reservations for the first class. Being State guests, we boarded last to find no first class seats vacant. Even Morarji could get a seat in first class only because a Pakistani civil servant vacated his seat for him saying, 'Hum itni to apki izzat kar sakte hain.'[2] In Rio, while I kept vigils writing speeches, I was under heavy medication. By the time we reached Paris on the way back where we halted, I was diagnosed as having pneumonia and even more heavily drugged. I was laid up for several weeks with one relapse and it was only my wife's untiring care and effort that saw me through.

The period of my illness was not without some lighter moments. Since Jagannathan was to leave for Washington, a new Economic Secretary had to be found; and it was rumoured that my name was recommended. It drew sharp protests from some IAS and ICS officers and many delighted in carrying tales to me and my wife. I was too weak to tell anyone that I did not really care much. In fairness, some of those who protested sent me a

copy of their representation to assure me that they had nothing against me but were fighting for their own rights and the rights of their service. Only ICS officers had been Economic Secretaries till then. Most of them were unwilling to surrender this citadel, and the IAS officers were only too keen to conquer it. Besides, I was all of 43—hardly an age to be a Secretary. Mrs Gandhi decided to wait till she had a chat with me.

My meeting with her was characteristic. She did not say she herself wanted me to be Secretary. This was recommended to her, and there were representations against it. For her, nothing was by merit and everything had to be a favour granted by her. I told her I was happy being a Chief Economic Adviser, and I had no ambition to be a Secretary. I was not biting; I was not pleading my case. After a while she said that one compromise suggestion was that I be made a Special Secretary for some time till things settled down, and Secretary later. She said she did not know what the difference was and was told there was really none and that I would have independent charge of the Economic Affairs Department in any case. I told her that if she thought I was 'special' among her secretaries, why should I object? She laughed, paused for some time, and then proceeded to tell me how she respected Morarjibhai for his ability. But she thought he was rigid in some ways and that someone to soften him was required in his vicinity. She asked my views on a number of points. Obviously, she made conversation because she wanted to make up her mind about me and ensure that I would not just be a Morarji man.

In due course, in December 1967, I was appointed Special Secretary with independent charge of Economic Affairs and assumed charge in January 1968. D.S. Joshi, the Cabinet Secretary, saw no point in calling me 'special' as I was to have an independent charge and would in any case have the same salary and seniority as if I were Secretary. He warned me that I should watch out that no other Secretary in the Ministry poaches on my territory—a necessary warning as it turned out. Morarji, Haksar and even Sheshan[3] advised me from time to time to remind Mrs Gandhi about dropping the 'special'. Sheshan even said she had kept the file with her and was only waiting for me to broach the subject. But I was determined not to ask a favour—and I was in any case at no disadvantage as a 'special'. It took, I think, two years before I was deprived of my adjective.

The change from Chief Economic Adviser to Special Secretary did not make all that much difference to my life. Much of my time was spent in dealing with external economic matters, notably negotiations and statement of our needs and the justification of our policies.* But there were some important differences. For one thing, I had now many visitors from Indian business—both public and private—who wanted something done or undone. In a way, the buck stopped with me at the official level when it came to economic policy and allocation of funds, particularly foreign exchange. At first I resisted this additional claim on my time. But Morarji set me right. My visitors spent a great deal of time and effort in trying to see me. They would not do so unless they had a genuine reason. Besides, they had experience of the kind which I did not, and I could learn by interaction with them. It was also my duty to be responsive to the demands of those on whom economic policy had a real impact. Over the years, I have learnt much by following this advice and have not turned down a single request for a meeting.

Individual decisions take much time and may involve more judgement on specifics rather than on issues of policy. Within the framework of given policies, there is a great deal of grey area and uncertainty about facts, and the consequences of the same action differ according to the ability and integrity of those who perform it. Economic administration is important and difficult precisely for this reason: it requires quick judgement and decisions on these grey areas and uncertain facts, on whom to give the benefit of doubt and on an evaluation of the persons one is dealing with. Political considerations also come in. And the issues that come up

*London, 19 May 2000.

are largely those of discretion rather than of rules and yet are not frivolous or altogether subjective. When Dr Kurien approached us with his plans for Operation Flood, many objections were raised on the file. I could not claim to know all the facts or quantify the uncertainty surrounding them. Ultimately, one went by faith in the man, his track record and weighing the costs and benefits. The same was the case when J.R.D. Tata came with his plea for the purchase of Boeing 747 for Air India. In both cases, I promptly weighed in their favour much on my own strength, for which both showed great appreciation. On the other hand, when a controversy arose about the purchase of planes by Indian Airlines with charges of bribes by rival firms, I had to set up an expert committee to make a cost-benefit comparison despite my high regard for Bharat Ram who was the Chairman of Indian Airlines at the time. There are also sensitive matters like allocation to defence or the atomic energy commission where it becomes entirely a one-to-one interaction—first between me and the Secretary concerned and then between me and the Finance Minister. Much of my time went in such decisions or mediations. Some of them were frivolous but took time and tact. Thus when Vikram Sarabhai wanted his flat in the new atomic energy residential building in Bombay to have some special features which Morarji was bound to find extravagant, I had to advise Vikram to add one or two requirements which he could do without and which I could advise Morarji to cross out. I knew he would want to cross out something as he thought Vikram had the tastes of a rich man—which was true. But Vikram deserved a residence to his liking. And there was some trust between Vikram, myself, and the Minister. Without some personal chemistry and trust, sensible economic administration is not possible.

I was also to discover that the Economic Affairs Secretary had responsibilities much beyond external economic relations and the Budget. Apart from the fact that this Department had a finger in the entire pie of economic policy, our Ministry was also a big employer and an entrepreneur. As the junior-most Secretary, I had to assume the role of the Chairman of the Joint Consultative

Committee of the Ministry, a sensitive role where I had at times to disagree with my senior colleagues and agree with the staff point of view. The staff included thousands of income tax and excise officers, those involved in regulating opium cultivation and trade as well as the vast array of clerical and other staff. This was good training for dealing with unions in later years. The Department of Economic Affairs even ran some enterprises like the Kolar Gold Mine (remember, gold has a mystique of its own and could only be entrusted to the finance man). We were setting up new enterprises like the Hoshangabad Security Paper Factory. The Economic Secretary then also had to be a bit of an entrepreneur and employer.

The membership of the Atomic Energy Commission with exclusive responsibility for Finance was an added burden but also a special bonus. It meant dealing with complex issues mostly on my own, negotiating in Canada or Brazil on matters far removed from aid and visiting sites in India which made little sense to me. It also brought me very close to some of the finest persons in public life such as Vikram Sarabhai and J.R.D. Tata. Along with the Atomic Energy Commission came the involvement in all parallel institutions with a similar parentage or purpose such as the Tata Institute of Fundamental Research, the Space Commission and even the Tata Cancer Hospital. The Economic Secretary was also the Honorary Treasurer of the Indian Red Cross which required hundreds of signatures for approval of accounts. The shades of Empire still persisted.

The Budget for 1968 has left little mark on my memory; and I do not think there were many significant new initiatives taken then in regard to economic policy. That period was not one of experimentation, but of consolidation. There were two exceptions: C. Subramaniam's remarkable achievement in ushering in the Green Revolution was one. It was not just a matter of importing seeds from Mexico or Manila. Even that was a bold decision, considering the apprehensions loudly expressed about the strange

seeds destroying Indian genetic material, introduction of new plant diseases and the like. Our own agricultural research facilities had to be substantially increased, extension work organized, arrangements made for the supply and distribution of fertlizers and for attracting foreign capital in this industry, major and medium irrigation, particularly lift irrigation and tube wells taken up on a large scale, and remunerative prices guaranteed to farmers while strengthening public distribution to take care of the interest of poor consumers. The Ministry of Finance had always opposed guaranteed prices and government purchase of all grain offered at these prices—out of fear that vested interests would push up support prices unreasonably and fuel inflation. But these fears were now set aside in the context of impending food shortages. While subsequent events have justified our fears, they have also fulfilled the hopes of those who created this new structure of food production and food trade.

The other innovation was the so-called social control over banking. The criticism that private commercial banks in India catered only to the needs of their industrialist owners and neglected the credit requirements of agriculture and small industry and trade had been around for many decades. The cooperative movement and the nationalization of the Imperial Bank had helped, but not much. Leftist opinion was clamouring for nationalization of banks, and Morarji's refusal to countenance this had made him a target in some Congress circles. Something had to be done and Gadgil encouraged the trying out of social control, which meant setting certain social norms for bank credit to agriculture, small industry and so on, and making the banks adhere to these norms. This meant making some sort of a credit plan by the Reserve Bank with targets or norms for overall credit increases across major banks, and the allocation of this potential increase to different users. I was myself not very involved in this exercise, although our Ministry was. Much of the work in Delhi was done by V. Pai Panandikar who had joined Morarji's staff as an adviser and by M. Narasimham in the RBI. Even if the idea was to deflect attention from nationalization, social control was an idea well conceived—and like many

good ideas, carried within it the seeds of political abuse as became clear later on. The methodology of credit planning was initially applied as the guiding star after nationalization. But soon, credit planning was replaced by credit melas just as project planning was being replaced in Delhi by arbitrary contracts and decisions to fill party or personal coffers.

Before accepting the position of Economic Secretary, I had told Morarjibhai that I would not like the new assignment to come in the way of something I valued greatly—the opportunity to attend international or national conferences and to write papers for them. These encounters gave me time to look back on things, to exercise my thinking and writing muscles and to get to know interesting people. By and large, I kept up with this practice throughout my official career. Just about the time I became Secretary, I had written a rather sharp paper in an agonised mood on 'Aid Relationship' for a conference organized by Barbara Ward.[4] I had written it in one feverish go late into the night to reflect my sentiments on our experience with devaluation and to question the current liberal fashion of using aid to improve economic performance and indeed to use it both as a prize for good performance and as punishment for the lack of it. What went with aid was not just pressure on national governments but also an attempt to separate sheep from goats in national administration. The exercise clearly favoured dictators over democrats who had to think about political support before making promises.

The truth was that the ardour for aid had abated in the hard post-Kennedy years, and performance calls were becoming shriller and shriller, and performance criteria stricter and stricter. Apart from the inevitable ideological bias in those criteria, there was inequitable application to suit political compulsions of the donors. I likened this policy to 'letting crime fit the punishment' because the aid to be given seemed to be decided on political grounds and all that remained was to justify the level by defining suitably the

sins of non-compliance by the respective recipients. I could not attend the conference. But my paper caused quite a stir making people like Robert McNamara unhappy that I was undermining their work, and several others like Paul Streeten telling me that they were glad I had written in that vein.

At the end of 1967, I gave my address as President of the Indian Economic Association at Calcutta on 'Limits of Economic Policy'.[5] It was my first attempt to recapture what I thought of economic policy at the time—and my views have not changed much. A similar recapitulation of my views on 'Trade and Development', germinated in my Ph.D. thesis and matured by my subsequent writing and experience, was attempted in a lecture given in Cambridge in 1972.[6]

Perhaps the most satisfying excursion at this time was attendance at the conferences in New York on International Monetary Reform organized by Sidney Dell of UNCTAD which were attended by several distinguished economists like Lord Kahn and Nicky Kaldor. It was at one of these conferences that I kept up all night at Tudor Hotel to present my ideas on the feasibility and desirability of creating an international reserve asset which needed no backing except the will of the international community. This paper was much commented upon and ultimately found its way in the Library of Congress where, I am told, my authorship is acknowledged. We recommended many things beyond the creation of an international monetary asset and most of these were later adopted by the Fund, albeit in a truncated form.[7]

One fall-out of these meetings was that I came to know well a Russian official called Alkhimov. I had, in my paper, used the expression: 'a substitute for gold'. He made fun of me the next day and said he thought I was a friend but did not know that I was to deprive him of all self-respect for ever. He said 'Alkhimov' meant an 'alchemist' and his ancestors had tried hard to find a 'substitute' for gold for ages but in vain. He went on to say that now, to his surprise and dismay, his Indian friend had found the substitute! Later, when I was at the RBI and when he had become my counterpart in Moscow, this friendship enabled us to settle amicably the long-standing controversy about the rupee–rouble rate.

Alkhimov was known for his ready wit. Sometime before our encounter, he had made substantial purchases of wheat for his country from the US at very low prices just before prices shot up considerably. He was accused of sharp practices and there were demands that the contracts should be cancelled and renegotiated. At one news conference, he was asked for his reaction and replied immediately that he was all for renegotiating the deal and added: 'Among friends, if there is unhappiness, we should reverse our steps. You return Alaska to us and I will cancel the wheat contracts.'

In the meanwhile, Morarji was facing increasing attacks from the left wing of the Congress Party, led in particular by Chandrashekar. Apart from Morarji's so-called conservatism, the influence of his son Kantibhai also came under attack. There were charges of undue influence as Kantibhai lived with Morarji in Delhi. Rumours had it that Mrs Gandhi was not averse to belief in those charges. On one occasion, I took courage and advised Morarji to ask Kanti to return to Bombay. I was prepared for the worst. Instead, I was told: 'My relations with my children have not been happy and it is not easy for me to talk things over with them. You are Kanti's age. Why don't you speak to him yourself?' I did. The response was not heartening.

*Towards a Congress Split**

The question of nationalization of banks did come up at a meeting of the National Development Council—I believe early in 1969. We knew some Chief Ministers would raise this question. Both Morarji and Gadgil were against it and wanted a fair trial for social control. But Morarji was getting a bad name for his point of view, and I advised him that he should ask Mrs Gandhi to respond to this matter at the NDC meeting. After all, if she wanted

*London, 20 May 2000.

to nationalize the banks, she should say so. If not, she should not hide behind her cloak of silence. At the meeting, Mrs Gandhi said clearly that she was not in favour of nationalization of banks, that we had yet to make a success of what we had already nationalized and that there was little point in taking on new responsibilities. Besides, social control must be given a fair trial. In the light of subsequent developments, I have a suspicion that this matter was deleted from the minutes of the Planning Commission. Differences on this matter were also the source of Mrs Gandhi's abominable treatment of Gadgil in the months to come.

Morarji travelled a great deal in 1968. I remember a trip to Australia when we stopped in Singapore for a day or two. Lee Kwan Yew and Morarji got along well and we had an excellent exposition from Lee Kwan of his economic and political philosophy which can at best be described as 'economic efficiency and social welfare achieved by market forces and dictates from a benevolent patriarch'—not quite a dictator because of the superstructure of democracy, but an autocrat all the same, albeit, largely approved by the people. I remember in particular how he said he tackled the housing problem. The State built several blocks of flats for workers and the lower middle classes and rented them out at slightly concessional rates. But people in each block had to organize into a kind of society to ensure cleanliness, proper maintenance and enforcement of good conduct and regular payment of dues. Each group of flats had service areas with shops which were rented out on normal commercial rates which in turn provided funds for proper maintenance of the whole complex. There were no theories, but a practical combination of State action, popular cooperation and participation, management by mutual surveillance and capitalist profits.

The visit to Australia was a great success and Morarji and the Australian Treasurer[8] got on so famously that the Treasurer and his pretty young wife invited us to spend a couple of days at their country estate. If I am not mistaken, the Governor-General of Australia then had been a Governor of Bombay at some stage. Later, at the Bank–Fund meeting in Washington, we had some

apprehensions about the US prevailing on the Bank to take a tough stand against us on some issues. We were canvassing support from various countries. When Morarji met the Australian Treasurer, the latter informed him that he had already told the Americans and the Bank that the Australian Government fully supported the Indian stand—and this was all the more noteworthy as it was in sharp contrast to the views of the Australian Executive Director who was vociferous in his criticism of India.

An equally memorable visit was the one to Germany where Morarji was invited as a State Guest by his counterpart, Karl Schiller. There were cordial meetings with Willy Brandt, Schiller and others and some sight-seeing to boot. Our last day was spent in Hamburg where I played bridge one afternoon with Morarji as my partner and Biju Patnaik and the Indian ambassador, Khubchand, as our opponents. The wily Biju knew Morarji played bridge and liked to win and he suggested that the *Gujjus*[9] should be partners as he did not want to take any risk of offending the Minister. As luck would have it, our team won every time: Khubchand was so anxious to please the Minister (or so optimistic, like most Sindhis) that he grossly overbid, and we simply doubled and redoubled and scored points.

Morarji's popularity among foreign governments also cost him much at home. His visits and the attention given to him were pointed at as his attempts at getting foreign support or attempts by like-minded Western governments to enhance his image and boost his chances. The cold war had its echoes in India's internal politics too. That the foreign governments might simply be ensuring their bets rather than betting on any particular horse was regarded as too naïve thinking.

I believe it was on our return from Germany, at the Rome airport, that an Air India officer informed us that Indian newspapers were full of reports that Morarji and Mrs Gandhi were supporting rival candidates for presidentship as a friendly President might swing the succession in favour of one or the other in the event of a split or a challenge. Morarji explained to him patiently that such rumours were unfounded and that under the Indian Constitution,

the President had no powers or influence in the choice of the Prime Minister. But there was substance in the story—at least in the sense that the issue of presidentship ultimately led to the split in the party. By the time we reached Bombay, the atmosphere at the Bangalore Congress meeting had become sufficiently tense for Morarji to proceed straight for Bangalore from Bombay instead of going to Delhi as previously planned. The drama of presidentship was dragged on for a few months more. But the die was already cast.

By that time, Mrs Gandhi had made important changes in her entourage. P.N. Haksar had taken the place of L.K. Jha as PM's Secretary and L.K. was sent to the Reserve Bank. After some time, P.N. Dhar also joined PM's secretariat. D.P. Dhar was an important adviser. In addition to this Kashmiri pundit triptych, there were others who fancied themselves rightly, or wrongly, as members of the kitchen cabinet. What was not in doubt is that Haksar managed to concentrate enormous powers in the PM's Secretariat and that his intellect contributed much to Mrs Gandhi's tactics and strategies. He was accepted as Mrs Gandhi's alter ego, and by most as Mrs Gandhi's tutor, mentor, and sole confidant—a reputation that cost him dear in the days of the Emergency. Both he and Sanjay could not be powers behind the throne; and his allergy to Sanjay meant that he had to be humbled and ousted.

My own opinion of Haksar is more favourable. He may have been all that was rumoured. But he was very able, and in my experience mostly fair and judicious and patriotic. I also found no particular ideological obsession in him. He may have been drawn to leftists as friends and companions. But he understood the compulsions of the times and was too shrewd not to understand the weaknesses of individual leftists as well as rightists, and was ready for practical compromises. If he disliked the Americans under Nixon and Kissinger, he had much reason to. I cannot fault him on his dealings with me as Secretary. In fact, he was very supportive—may be, because I was neither ICS nor IAS member, both services never favourites of his. P.N. Dhar's presence may also have softened him ideologically, though both shared the Kashmiri's penchant for *mutsaddi*.[10] When a secretary in the Ministry of Finance

tried to trespass on my territory, Haksar saw to it that he was immediately transferred. He pleaded for my being made a Secretary as soon as possible. Later, when I had to fight for my turf after the creation of the Banking Department, he was impartial and fair. After his experience in the Emergency, he became positively fond of me and during the last years of his life, he always treated my wife and myself with great affection. Pitambar Pant's closeness to Mrs Gandhi also helped. Pitambar was soon disillusioned about Mrs Gandhi and while he remained loyal, he was too honest a person—and too strong and proud—to endorse every whim and fancy of Mrs Gandhi. Altogether, the changing climate left me virtually untouched—although I was still known as Morarji's man in many circles and certainly in Mrs Gandhi's mind.

Once the fundamental battle was resolved in her favour, Mrs Gandhi was ready for the kill. The final blow—and the declaration of a formal split and war—came, I believe, soon after the meeting of the NDC referred to earlier. I remember being summoned to Morarji's office together with other Secretaries in the Ministry. We were informed that Morarji had just received a letter from Mrs Gandhi divesting him of his post as Finance Minister, but retaining him as Deputy Prime Minister without any portfolio. While we were with Morarji, the news came that Mrs Gandhi had assumed charge as the Finance Minister. Some people present tried to advise Morarji that there must have been some misunderstanding and that he should call on Mrs Gandhi and clear the air. It was clear to me that Mrs Gandhi wanted Morarji out and the only honourable course for him was to resign and leave the Government. Morarji said he agreed with me and immediately sent in his resignation which was promptly accepted. Within hours, Morarji and his staff cleared out of North Block. I was sad and furious; we had worked so hard to bring the two together and things had worked out well as far as the revival of the economy and our external relations were concerned. What earthly purpose would be served by the split? That evening, P.N. Dhar came to see me and I made no secret of my feelings. Pitambar also came, and he too was sad. What we had done together was undone.

The next day I was sent for by Mrs Gandhi. There was nothing unusual in the Minister summoning a Secretary, and I told her about some of the urgent issues that needed her attention. I also told her that we would, in consideration of her other responsibilities, be sparing in the files we sent to her and I asked incidentally how long she intended to keep charge of the Finance portfolio. She listened carefully and then asked suddenly, 'Is it true that you are very unhappy and would like to leave the Government?' Obviously, Dhar Saheb had told her the gist of our conversation including my past record in resigning. I replied honestly that I was unhappy for reasons she would understand but that I had no intention of leaving as long as two conditions were satisfied: our bona fides were not doubted and we were taken into confidence about the intentions and objectives of the Government without which we cannot give relevant and careful advice. If I had known what was coming I would have added a third one: that what we were expected to do should square with our ideas of right or wrong. Mrs Gandhi said nothing directly to the point; she neither assured me nor chastised me. She proceeded instead to repeat what she had done earlier—praise Morarjibhai but add how rigid he was and that he did not understand the times. She asked me to send more files than we did to Morarji and to ask my officers (and myself) to make our notes detailed, giving all background since, unlike Morarjibhai, she was not an expert in the field. We need not worry about the files getting delayed; she could work hard and the files would come back to us in time. After some questioning on a few issues, as I was preparing to leave, she said: 'You asked me how long I propose to keep this portfolio. As long as it takes you to initiate me into the intricacies of finance. I do not want anyone to say that the PM of India knows nothing of finance.' I knew I had been examined and had passed the test.

She was true to her word. She worked hard, was quick to grasp and very responsive to our advice. It was remarkable how much and how quickly she would assimilate and decide in a day. She made it a practice to meet three or four of us for two hours (9–11 a.m.) twice a week just before her question hour in Parliament. Those sessions were like classroom meetings where there was great

informality and humour. I remember my once telling her that tax evaders should never be jailed because they must be left free to earn to be able to pay the taxes—and she actually laughed aloud. There was no arrogance, no imperiousness, no impatience; just a discussion among equals and readiness to learn. I can say without hesitation that these sessions are among my happiest memories of work in Government.

Bank Nationalization

It was, I think, later in July 1969 that I was sent for once again. No one else was present. Without any fanfare, she asked me whether banking was under my charge. On my telling her it was, she simply said: 'For political reasons, it has been decided to nationalize the banks. You have to prepare within 24 hours the bill, a note for the Cabinet and a speech for me to make to the nation on the radio tomorrow evening. Can you do it and make sure there is no leak?' There was no pretence that this was not a political decision, and the message was clear that no argument from me was required. I assured her we will keep to the time-table and keep the secret. I summoned courage, however, to make two suggestions: to leave the foreign banks alone, and nationalize only the major ones. The former was intended to avoid sharp reaction abroad; and the latter because the purpose would be served by taking only the major banks and leaving the scores of small banks alone. She immediately agreed and added that she could trust the details to me.

This was a daunting task if ever there was one, and more so as I could not take into confidence even my closest associates. I had to ask L.K. Jha to come to Delhi immediately without telling him why—the Governor of the RBI could not be kept out of this major issue. I also asked him to bring with him R.K. Sheshadari, an RBI officer who was with the Ministry earlier, with a copy of a note he and I had prepared on banking. Fortunately, T.T.K. had once asked the two of us to prepare a draft legislation for nationalizing banks and I knew Sheshadari had kept the only copy as his was the main contribution. L.K., I am sure, understood.

The three of us worked through the night: L.K. and Sheshadri in the RBI Governor's flat in Delhi, and I in my house. There was no question of using the office or collecting references or consulting others. I drafted the Cabinet paper and the speech for Mrs Gandhi and they prepared a draft bill. Fourteen banks were selected for nationalization as between them they accounted for some 85 or 90 per cent of the deposits. I had to provide all the justification in simple terms for the Cabinet and the country. I was afraid that the announcement might generate fears about nationalization in other sectors and create a major financial crisis. On my own, I inserted a sentence in Mrs Gandhi's speech: 'This is not the first step in a new wave of nationalization. This, in fact, is the culmination of the process which began with the nationalization of Life Insurance and the Imperial Bank to occupy the commanding heights of finance.' The idea was to link with the past to take away the revolutionary edge, and even more to assure that no more nationalization would follow. Not a word of what I wrote was changed by Haksar or Mrs Gandhi next morning—including what I had added on my own initiative. I think this, and the decision to exclude foreign and small banks, softened the blow. The Cabinet was a walk-over and the popular response in the country was one of open welcome. Even those affected had expected something of the sort and were anxious now to salvage what they could. It is remarkable how momentous decisions are made in the heat of political struggle. After this, Mrs Gandhi was heralded as the angel of the poor and she made the most of *Garibi Hatao*.

The legislation was challenged and had to be revised; and this created a mood of changing as little as possible to avoid further judicial problems. Thus, all the banks and their management, staff and structure remained as they were. Only the ownership changed and the only operative instrument for change was 'social control' or credit planning, albeit buttressed now by conscious government decisions from time to time, like the Twenty Point Programme.

This return to the spirit of the status quo was, in a way, a pity. It prevented a major restructuring of the banks to make them more efficient and more responsive to social needs. I had myself prepared a note outlining such a restructuring. The idea was to allow only one or two major banks to remain as all-India banks, catering to the wholesale market for credit so to speak and with a monopoly of foreign exchange business. They could then compete on equal terms with foreign banks, be sources of innovation and enable a better implementation of foreign exchange control. The rest would be reorganized, merged, and re-packaged to create several entities which would work in specific regions and concentrate on agriculture, small industry and trade and the hitherto credit-starved areas. There would be two or three regional banks operating in each region so that there would be some competition. At the same time, there would be greater economy as some branches could be merged and excessive competitive expansion avoided in the future. Above all, the emphasis would be on local needs and exploiting local opportunities: two cultures living together and interacting, so to speak. But such ideas were not even discussed, so great was the anxiety to make nationalization stick legally and politically.

For me, one consequence of nationalization was controversy once again about my jurisdiction and that of my department. A new Banking Department was created in the Ministry under A. Bakshi from the RBI, an old leftist and acerbic friend of Haksar who could obviously be more relied upon to run nationalized banks than L.K. or I.G. There was naturally an attempt to give as much power as possible to the new department on the grounds that a new presence needed extra support to enable it to settle down and be accepted. Thus, initially, the RBI was to be made the exclusive responsibility of the Banking Department, giving its Secretary quite a hold over the Bank and future appointments in it. The Cabinet Secretary, D.S. Joshi, was aghast at the proposal as was L.K. I took up the matter right away with Haksar (who I knew had acted on the advice of Bakshi). Haksar, as I have said earlier, was fair and impartial in working out a solution. Administratively, the RBI would be under the Economic Affairs Department whose Secretary would remain on the RBI Board. The responsibilities of the Banking Department were clearly defined and related to allocation of bank credit and management of nationalized banks. The larger questions of monetary policy, management of government debt and foreign exchange were to be with us. Thus, what we had

we retained, and what was relatively new after nationalization was entrusted to the Banking Department.

There was to be coordination between the two Departments and the new Chief Economic Advisor, Ashok Mitra, was to be responsible for this aspect. This was most welcome to me. I knew Ashok well, warts and all. We had a long-standing friendship and I knew that he would be an honest broker between Bakshi and myself. In fact, his choice was entirely at my suggestion and even Haksar was surprised when I recommended his name for the position of Chief Economic Adviser. My reasoning was simple: he was very able, could draft well and quickly, his leftist image could do no harm to the Department and my personal relations with him would keep him away from mischief. In any event, given his track record, we knew he would not stay with us for long. The coordination with the Banking Department—between the Bengali leftists—left me free to devote my time to my main responsibilities from which Ashok in fact became largely divorced.

V. K. Ramaswami

The necessity to appoint a new Chief Economic Adviser arose because of the ghastly accident that killed Ramaswami. His chair caught fire at night presumably from a spark from his cigarette. He was not aware of this, went to bed and was asphyxiated by the smoke. I was woken up next morning and rushed to his house to witness this tragic and gruesome sight. His death was a great loss to the country and to economics in India—both to economic policy and economic analysis and research. It was equally a great personal loss. Our relationship had begun rather awkwardly. When I was in my third year B.A., Ramu was in his first year B.A. at Baroda College, and seeing the Dewan's son arrive everyday in a big car with escorts did not endear him to me. We never met, but I had then all the resentment of a poor youngster for rich people. To add to this, when my teacher D. Ghosh took me to V.T. Krishnamachari, the Dewan, to introduce me to him and to plead for a state scholarship for me to go to Cambridge after my B.A. degree, the

father's reaction shocked me: 'He should go to Oxford, not Cambridge, after finishing his masters degree. Ramu would be ready by then to go to Oxford and I.G. could be a good companion for him'. I was obviously only a means to an end. Our paths never crossed when we were in England and only rarely when he was with the RBI. His choice as the Economic Adviser for the Commerce and Industry Ministry in preference to Krishnaswami was also suspect in our eyes as allegedly the result of the influence of his father now Deputy Chairman of the Planning Commission.

All this prejudice on my part disappeared as I came to know him better; and after 1965, he became a very good friend and a valued colleague. He used to feel even more at ease with my wife. He was under some personal strain at the time, and our house was a haven for him. Even Sir V.T. once invited me to tea to tell me that he was worried about his dearly loved son, that he knew Ramu thought a great deal of me and that I should help him in his personal predicament. Such is filial love that it humbles all pride. The tragic loss was difficult to take. When I got a chance to pay my tribute to him while giving the Ramaswami Memorial Lecture, I said something which my friendship with him had taught me. We all think children from poor families are at a disadvantage in life. But rich children also have their cross to bear. The world seldom gives them credit for what they rightly deserve. Their achievements are often discounted as results more of good fortune or influence and favouritism than of merit or hard work. I could have added—but did not—that a privileged childhood does not necessarily prepare you well for dealing with all the vicissitudes of life.

*Mrs Gandhi as Finance Minister**

By all accounts, the nationalization of major banks was a great success initially. Apart from the political dividends for Mrs Gandhi, it greatly increased popular confidence in the banking system and thus increased the mobilization of private savings through banks.

*London, 22 May 2000.

The savings so mobilized were also used now for supporting public borrowing as well as for meeting hitherto neglected genuine credit needs. The rot started with the Emergency; and what political opportunism started was compounded by bank staff of all grades. With nationalization came the entry of national unions owing allegiance to different political parties, mostly the Congress and the left. Shielded by political support, the bank staff proceeded to create for themselves a vast superstructure of perks and privileges under which they could define and limit work, enforce overstaffing and generally encourage indiscipline and incompetence without any fear of being held accountable. Merit went by the board as did customer service; and seniority and closeness to political power held the sway. Fraud could not be far behind. Is such a denouement inevitable in all circumstances so that public ownership is eternally damned? Or is it particularly the result of fragmented and bitter political struggles in a democracy which survives on votes and the power and muscle to attract them? There is truth in both the propositions, and they are not mutually contradictory. The difference is only in the time frame. Private ownership too has its infirmities. There is no such thing as perfectly competitive markets divorced from political realities. The choice is of the lesser evil—which may not always be the same at all times and in all places.

The only other important event under Mrs Gandhi's stewardship of Finance was the 1970 Budget. It was not revolutionary, but routine and cautious and on traditional lines. The only exception to this was the clubbing of the income of husband and wife—a strange and unusual innovation from a woman Prime Minister, but characteristic of Mrs Gandhi. Needless to say, the provision did not survive for long on the statute book. Mrs Gandhi's Budget speech was praised for its humour and wit—for which I claim credit, as once again, she had changed not a word from my draft. I remember the introduction to the proposal for clubbing: 'What Fate has united, let no man rent asunder.' The increase in the duty on liquor was described as 'a gesture of personal, if not political, rapprochement'. Everyone knew what the reference was.

The 1970 Budget was the only one passed as proposed without any proposal being dropped or modified because of opposition in the House. I remember urging on Mrs Gandhi that the practice of yielding to pressure invited only more pressure and that she should use her Prime Minister-cum-Finance Minister status to set a new precedent of 'no change'. Such advice was pleasing to Mrs Gandhi and she resisted all attempts to have the proposals modified.

On the day before the Budget was to be passed, I got a note from her that one particular proposal would have to be modified as the opposition to it was too strong. I was asked to prepare an alternate draft. I did—but also gave another draft which would have meant virtually no change. In her winding up speech, she made no announcement of any concession; and when we asked her if she forgot about it, she simply said: 'No. But, as I was speaking, I remembered what you had said about the PM setting a precedent, and I thought—well, let us see.' That was vintage Mrs Gandhi.

Soon after the Budget was passed and almost a year after she took over as FM, she appointed Y.B. Chavan to take over. Before referring to his time, mention must be made of a dark spot on Mrs Gandhi's career—her treatment of Professor Gadgil. In a nutshell, Gadgil was too honest a person for Mrs Gandhi's liking. He would not always suit her purpose. After Morarji's ouster, she must have decided to remove Gadgil too; and her resolve must have been strengthened by the fact that Gadgil refused to praise the nationalization of banks from the roof-tops. He could not do so, given his earlier stand in Government. With his background, he could not be averse to nationalization. But he was a man of principle and would not support it merely as an expedient tactic. Whether he was finally asked to go or whether it was made clear to him that he had outlived his welcome and forced to resign, I do not know. But I know how unhappy Gadgil was, although he never gave vent to his unhappiness. Pitambar, who was as upset by this development as I was, invited Gadgil to stay with him till he could

finalize his departure from Delhi. But Gadgil decided to immediately pack up and leave. Pitambar and I went to Delhi railway station—he was taking the Frontier Mail to Bombay. Just a few people came to see him off. Gadgil fainted on the platform. He was obviously greatly agitated inwardly. We pleaded with him not travel that day. But he would have none of it. Not one more day in Delhi, he must have thought. Ultimately, we persuaded his secretary to jump into the train and accompany Professor and Mrs Gadgil to Bombay. He did. But at Mathura, Gadgil prevailed upon him to return to Delhi on the plea that he was now well. As it happened, he never reached Bombay. Thus came the end in a moving train of one of India's noblest sons with no one else but his wife to bid him good-bye. Fate punishes everyone in her own way; and Mrs Gandhi had more than her share of punishment. But I am not sure if those who conveniently kept away from saying good-bye to Gadgil in Delhi had any pangs of conscience. At the end of the day, Delhi honours no one, not even the rising stars of yesteryears. D.P. Dhar who succeeded Gadgil conducted himself with no great distinction.

Y.B. Chavan

As Finance Minister Chavan Saheb is generally regarded as a colourless person. But he was able, quick to grasp and, while attentive to our advice, not devoid of political sagacity or practical wisdom to put his own stamp on the decision-making process. He was a perfect gentleman, available at all times and not anxious to shirk responsibilities. What gave an impression of insipidity was that he was shy and a man of few words. He must have also been inhibited by the fact that Mrs Gandhi did not trust him fully and he could not have been sure of his position or independence. But for us, he was as good a minister as one could hope for in the circumstances. He was loyal to his staff; and one of his endearing habits was that he always read some book or the other whenever he found a little time, instead of indulging in idle gossip.

Soon after he took over, we travelled to Copenhagen for the Bank-Fund meeting which became memorable for the virulent

protests against McNamara for his role in the Vietnam War. Thousands of protesting students and their leaders like Tariq Ali descended on this town and milled around, singing and shouting. They were intimidating, if not actually violent. The Indian delegation was a particular target as we were large borrowers from the Bank and known to be friendly to McNamara.

We had a foretaste of this in 1968 soon after I took over as Secretary when the McNamaras came on their first visit to India after McNamara became President of the World Bank. He wanted to go to Calcutta as he had lived there during the War as a US army officer and was deeply moved by the conditions in the slums. He wanted to visit them again. The night before his departure from Delhi, we got word that the leftist parties had vowed not to let him enter Calcutta and had organized vast protest marches. When told about this, he very diplomatically replied that he was a guest, and it was for the hosts to decide where to take him. We had no choice but to take him, and my wife and I accompanied them. At the Calcutta airport, we were surrounded on all sides and the way to the town was lined with protesters. The Governor's residence in the centre of the city where we were to stay, was also surrounded. We had to finally get there in a helicopter. I never knew Calcutta could look so beautiful from the air at low altitudes—there is much greenery and many old buildings with ponds and gardens which lie hidden from sight by road. We conducted all our meetings surrounded by the crowd. But early next morning, McNamara was quietly driven to the slum areas and, once again, he was deeply moved by the continuing poverty, filth and disease. Such is the irony of life that the leftists were protesting against someone whose sympathies for the poor were no less, and whose actions perhaps more effective and eloquent, in reducing their misery. Little did they know that McNamara deeply repented for his past and understood at least one point the protestors were making about the brutalities of the Vietnam War for which the Americans undoubtedly were largely responsible. The protesters were unwilling to accept that individuals can change, even if nations and groups cannot, or can do so only imperceptibly.

*The Bangladesh Crisis**

By the time we returned from Copenhagen, the Bangladesh crisis was building up. The Pakistani aristocracy in the Punjab and in Sindh was not prepared to honour the results of the elections and allow a Bengali to be the Prime Minister. The resulting protests were brutally put down, inviting more protests and more army brutalities. For India, the mayhem—directed largely against Hindus and Muslim students, intellectuals and politicians in what was East Pakistan—meant a steady influx of refugees which soon became a flood and reached a level of some few million men, women and children. Getting some of the Muslim intellectuals like Nurul Islam and Rehman Shobhan out of Dhaka was no mean task and was greatly facilitated by the Ford Foundation. To add to our worries, the US under President Nixon and Henry Kissinger was hell-bent upon preserving Pakistan as one unit and spent more time and words in warning India against intervention than in urging the Pakistani generals to see reason.

We faced a daunting dilemma. We could not absorb ten million refugees and invite more without the economy of India, and particularly of West Bengal, being totally ruined and our internal communal harmony severely strained. Again, we could not invite the wrath of the mighty Americans who were threatening economic sanctions, not only by them but by their allies as well. We knew this would mean stoppage of aid, including aid in the pipeline, and perhaps freezing of our assets abroad.

The time was for cool heads and quiet diplomacy combined with firm resolve; and Mrs Gandhi rose to the occasion superbly. I was asked how long we could sustain a conflict if the sanctions were applied. I was able to say confidently that with 1000 million dollars in reserves and 10 million tonnes of foodgrains in stock—a measure of the revival achieved since 1966—we could easily manage for three or four months. We could also isolate the US in regard to sanctions by mounting a diplomatic offensive. In the coming weeks, I travelled all over the world explaining our plight

*London, 23 May 2000.

and asking for understanding. Such was the magnitude of Pakistani brutalities and the plight of the refugees that our pleas fell on willing ears. Even in the US administration, there were sympathizers. I could confidently say that with the possible exception of Japan, no country would follow the American example and that even the US may not apply extreme sanctions such as freezing of our assets. The enormity of Pakistani brutality and the strength of world public opinion were such that the allies could afford to displease the Americans. Our own low-key but passionate diplomacy could not have done any harm.

What we did not know then was that the US official attitude was utterly callous and selfish. Nixon and Kissinger had made up their mind to make peace with China, and Pakistan as an ally of both was acting as a go-between and using its good offices to bring China and the US together. The US could not afford to displease Pakistan. The prize of China was too big to allow the plight of the millions of refugees or the sentiments of millions of Bengalis to come in the way. So much for American principles. In fact, Kissinger visited Delhi on his way to Karachi (from where, I think, he went to China secretly) and at a dinner given in his honour, did his best to deceive us. Contrary to known American views, he pretended sympathy for our cause and tried to imply that the US, given time, would ensure that our purposes were met. The idea was simply to pursuade us to hold our hand till his China mission was achieved. He must have known that the Chinese—or for that matter, the Americans—would never intervene militarily and could not thus sway the outcome except by diplomatic pressure or duplicity. We did not know all his calculations then. But at the end of the dinner, when we tried to evaluate his remarks, both Haksar and I agreed that Kissinger was a consummate artist of deception and that his words could not be trusted.

In the event, things moved swiftly, Pakistan's military defeat was total and humiliating and Bangladesh came into being with Sheikh Mujibur Rehman as its first Prime Minister. It was the proudest day in Mrs Gandhi's political career. Henceforth, there was no question of a challenge to her authority. But the cost to the

economy was great. Although the refugees returned by and large, many stayed behind. The Hindus were not to trust Bengali Muslims readily. For Bengali Muslims, India was a land of opportunity. A new chapter of migration into India from Bangladesh began. This has not yet ended and has created a new set of tensions in the North-east where the indigenous people are up in arms against what they see as cultural annihilation by an alien people. That the Congress Party often turned a blind eye to this influx for electoral reasons has added fuel to the fire of insurgency. This particular outcome of the Bangladesh war was not obvious to us then. Pakistan had effectively sealed the borders for ideological reasons. Now that India had a friend in Bangladesh, the borders—difficult as they were to maintain in any case—became rather porous.

In 1972, on the eve of my trip to the UNDP in New York, I went to Harvard where L.K. and I were to give a talk at a dinner for Moynihan who was leaving shortly for India as ambassador. That dinner was memorable for two reasons. I have already referred earlier to my advice to Moynihan on liquidating PL-480 rupees. The second memorable fact about that evening was a remark by a neighbour of mine at dinner—I forget his name, but he taught labour economics at Harvard. He said, 'Dr. Patel, now that you are friendly with Bangladesh, I suppose the historical migration of Bengali Muslims into Assam and India's North-east will be resumed.' This had never occurred to me and I asked him what he meant. He told me about natural population and economic dynamics and how, under the British, a large-scale migration had taken place and this was interrupted by Partition. One understood better now Jinnah's insistence on treating the whole of eastern India beyond Bihar as a single unit or a loose federation in the event of partition. That was one reason why he called the Pakistan he got 'maimed, mutilated and moth-eaten'. Perhaps that was why the British wanted to divide Bengal—to unite the whole of the East and North-east under Muslim majority as a part of the game

of divide and rule. How little attention do we pay in India to history and to the understanding of geopolitical realities!

The Aftermath

Economically, the Bangladesh war left much repair and reconstruction to be taken care of. But politically, Mrs Gandhi's star rose and this was reflected in the results of the 1972 elections. But such are the vagaries of human nature that with triumph came hubris and the delusion. She could do what she liked and did not have to worry much about right and wrong. That ends justify means was perhaps a part of her make-up. In any case, the 1972 elections were the first occasion when great political pressure was brought to bear on me to do what I would not do. The Economic Secretary had vast powers at least of refusal;[6] and setting aside his views would not be politically expedient. The pressure came from L.N. Mishra who was Congress Treasurer, but everyone knew that the PM was backing him. The pressure took the shape of many files coming to me for clearance; to favour some firm or another for obvious quid pro quo. I was called on the phone at work or home, and his subordinates made imperious demands. I had no such experience before, and I was not going to begin a new and unfamiliar and unpalatable chapter in my life. My refusal to toe the line even brought some verbal hectoring from Mishra himself.

At one point, I felt that I was perhaps harming Chavan's future by my obstinacy. His position was vulnerable anyway. I went to him and told him, what was happening and asked him whether he would prefer that I sent the files to him for him to deal with rather than dispose of them myself. His response was forthright. He said I should carry on with the way I was handling matters. If I wanted to for any reason, I could also send a file to him for clearance. But in that case, I should on a separate piece of paper express my views and the reasons thereof. There was, he added, a third way. I could lock up the files till the elections are over. No one would ask for them after that. Who would say Chavan was colourless? How many ministers today would say this? And yet it is a reflection of the

times that Haksar once told me disdainfully: 'Chavan will do anything to remain in power. He likes to eat a chicken at every meal. Who is going to provide him that when he is not in power?' Such is the dynamics of power. Its fuel is cynicism.

There were noises against me after the elections, notably from L.N. Mishra. On one occasion, he confronted me in London in the presence of several officers and NRIs and said, 'Patel Saheb, you think so much about your policies. Why don't you talk to these people to see how wrong you are?' When I did, the issue turned out to be a comic one. The NRIs had complained that the Department of Economic Affairs was not giving a P form to Indian boys and girls who wanted to come to Britain to get married. I was surprised, because years ago I had been responsible for a change to make this possible. A friend of mine, Chitra Majumdar, who was Professor of English in Patna wanted to go to England to marry a British diplomat, and she was denied a P form as one's fiance was not defined as a near relative, only blood relations were. I had got this rule changed with the help of L.K. Jha who was then Secretary. Apparently, what happened was that the NRI would invite several boys to marry the same girl who would refuse them on arrival, making room for another boy and another P form. Obviously, a loophole had been found to admit young relations into the UK. The British had asked for tightening of the P form procedure; and the mandarins in the North Block had found the usual bureaucratic solution: the same girl (or boy) could refuse only one suitor, no more. In short, an NRI could generate at best two P forms, no more. I learnt a new lesson in economic administration.

It was clear to me that I could not survive in the government honourably. I was in my fifth year as Economic Secretary and the convention was that no one remained in the same job for more than five years. In fact, I had been in that position longer than any other previous incumbent. I had no doubt that, at the least, I would be transferred to some minor ministry and I had no desire to be a Secretary in any other ministry as it did not fit my professional credentials. I made up my mind that it was time for a change and told my wife who fully supported me in my resolve.

As luck would have it, an unexpected development took place in the summer of 1972. Rudy Peterson, who was earlier President of the largest American bank, the Bank of America, and who had just taken charge as Administrator of the UNDP, stopped by in Delhi on his way to Japan. His main purpose was to sound me out for the post of Deputy Administrator, with the rank of an Under-Secretary-General. I did not know Peterson, and learnt later that the suggestion had come from another Peterson (Peter) whom I knew. He was at some stage the US Secretary of Commerce or chairman of some committee to review aid. UNDP came under my charge as Secretary in the Ministry of Finance. But its aid was so limited that relations with UNDP were handled almost entirely at the level of a Joint Secretary. I never attended a meeting of their Governing Council. I expressed my interest provided the Government agreed. I knew Mrs Gandhi would be happy to see me out—which she was. Without much fanfare it was agreed that I would be given leave of absence for three years which could be extended by two years and that I could join the UNDP in December 1972 when I would complete five years as Economic Secretary. Thus, this very crucial change in my career came as a complete surprise, without any effort on my part, and without any canvassing by the Government which usually precedes high-level appointments in the UN system.

McNamara was unhappy that he did not know I was looking for a change. He would have liked me to join the Bank. I am glad I went to the UNDP as a Bank assignment would have been considered a wangle. By then, we had become good friends; and McNamara thought my family should become familiar with New York before I settled there. I had also to be a discussant at the Per Jacobson lecture that year during the Bank–Fund meeting, and I needed some free time to prepare my remarks. McNamara arranged for me to be a resident-scholar at the Aspen Institute of Humanistic Studies where I spent two or three very enjoyable weeks with my family just before the Bank-Fund meeting. The Aspen Institute is a remarkable venture of the biggest names in US industry. They and their families spend some time at the Institute to re-charge their 'humanistic' batteries and to have a holiday in luxurious

surroundings. There are lectures by visiting scholars, seminars, discussions on specific texts and interaction with resident-scholars. The idea is that business executives at the highest level should know of higher ethical and philosophical issues and should be exposed to world classics of religion and philosophy like the Gita or Plato or even Nietzsche and Marx and Shakespeare. My companion resident-scholar was Roy Jenkins and the facilities for reading and recreation were superb; the food was classic, too: you could only have salmon or trout or a beef steak!

I decided to be controversial and frank at the Per Jacobsson lecture. In 1971, Nixon had taken the bold step and made the dollar inconvertible and levied a 10 per cent uniform import duty to signify that he wanted the dollar, to be devalued. The declaration of inconvertibility in a way was phoney as the dollar for many years was inconvertible in effect. In theory, the US was committed to buy all gold offered at $35 per ounce and to sell all gold demanded at the same price. It did buy all gold offered at $35 per ounce; but it made it clear that it was not going to part with its gold in exchange for dollars. The result was that no country dared convert its dollar earnings into gold at official prices unless the US so wished, and all were obliged to go on holding dollars or to resort to the black market in gold which was illegal under Fund rules, so that the black market catered mainly to Russian or South African suppliers of gold and the trade in jewellery or illegal smuggling in countries like India. The US was thus having its way as usual. The formal inconvertibility was only a fig leaf behind which the intended devaluation was to be hidden. The Fund obliged, as usual; and a working group set up by the Fund concluded that the US should devalue by 10 per cent against all currencies (with gold valued appropriately in dollars for official purposes), that is, by exactly the amount announced by the US by its 10 per cent across the board import duty. What a coincidence!

I pointed all this out to illustrate international political realities and argued that international institutions were not always as objective as they should be. I wanted to imply that this erodes

their authority and that they should not be so preachy or vociferous in their policy advice to those not so powerful. As usual, we had to cover up our own infirmity in policy-making by being preachy ourselves! Only, we were audacious enough to preach to the rich as well.

Before returning to India, we spent a few days in New York ensuring admission for our daughter in a good school and exploring residential possibilities. 12 December was to be the date for my leaving the Government to join the UNDP. As it happened, I found myself in Brussels on the day, participating in a conference organized by the Atlantic Council. Arrangements had to be made for my handing over charge in the Indian Embassy in Brussels.

Thus ended some fifteen years of stay in Delhi of which fourteen were spent in the Ministry of Finance. They were happy and eventful years during which I learnt much. I was engaged and involved and gave of my best. In return, for the most part, I gained all the support and recognition and affection I could have hoped for from my colleagues and political masters. And, I think, we did render some service to the State. If we erred, we erred in good faith; and I could also say, as Sachin Chaudhuri had done, that when I left Delhi for good, I left by the front door and without any scars. They were very happy years outside the office too. Our daughter had arrived and was growing up well. My wife's transformation from an academic to a practising musician brought much delight and the company of a whole new world of artists and art lovers. And we made many friends in all walks of life. Our house at 11, Teen Murti Lane was the centre of much festivity and superb musical evenings—one memorable one was in honour of the Schweitzers. As a departure from normal practice, I invited all my staff, class four included, to a farewell party in our garden with our many friends, and the warmth of that evening was reward enough for all the work and vexation that had gone before.

Endnotes

1. V. Kurien was one of the pioneers of the movement for organizing co-operatives of milk producers in the Kheda district of Gujarat—a movement, which under his leadership, spread far and wide all over India in the years to come.
2. We can show at least this much respect for you.
3. Mrs Gandhi's personal assistant.
4. Columbia University Conference on International Economic Development, Williamsburg, Va. and New York, February 1970. Reproduced in the conference volume *The Widening Gap—Development in the 1970's*, Columbia Univ. Press, 1971. Also reproduced in my *Essays in Economic Policy and Economic Growth*, Macmillan, London, 1986.
5. Also reproduced in my *Essays in Economic Policy and Economic Growth*.
6. Opening address at the Ninth Cambridge Conference on Development Problems, St John's College, Cambridge, 19 September 1972. Published in *Trade Strategies for Development* edited by Paul Streeten, Macmillan, 1973. Also reproduced in my *Essays in Economic Policy and Economic Growth*.
7. I also participated in a seminar at the International Monetary Fund in June 1970 on 'International Reserves—Needs and Availability', see pp. 114–19 in the conference volume with the same title.
8. Equivalent to our Finance Minister.
9. As the Gujaratis are often called with a mixture of envy, affection and admiration by non-Gujaratis!
10. Diplomacy with delight in devising strategic games.

6

The United Nations Development Programme, 1972–7

The story of the next five years at the UNDP in New York does not really belong to this narrative. But a few things are relevant and worth a mention.

New Directions in Technical Assistance

I had spent a lot of time criticizing the Bank and the Fund, trying to liberalize their policies and contrasting the UN as a more democratic institution. The reality I encountered was disheartening. The UN institutions had little to do and were even more tightly governed by the member States. They soon became a source of jobs for experts or officials from member States who fought for the jobs, the major ones getting the lion's share. With not much real power and responsibility, bureaucratization ensued. The UNDP was not free from it with its very limited budget and vast mandate. It had to operate in some 180 countries and provide technical assistance in all fields: health, education, industry, commerce, communication, economic policy and all the rest. And it also had a role in problems that transcend national boundaries. The staff was good but demoralized; and donor governments had forced self-serving policies that we had successfully opposed in the Bank. Thus, when I arrived at the UNDP, an expert could not be sent to his own home country.

UNDP funds could be used only marginally for equipment in any case. The Governing Council, a large body of 40 odd members, met twice a year for one month on each occasion—once in Geneva and once in New York. This meant that everything in the UNDP came under minute scrutiny by a host of junior officials who were often ignorant and did not even know their governments' mind in every case. The Agencies were fiefdoms and fought for their share of the UNDP pie without wanting to be accountable.

I cannot say I achieved much. But through an initiative called 'New Directions in Technical Assistance' on which I worked hard—diplomatically and otherwise—something was achieved. But basically, not much could change as the whole idea of the institution was flawed: it was born out of a desire to silence the developing countries by throwing a few crumbs at them. To make things worse, we ran into a financial crisis for the usual reasons: we were encouraged first to spend more as there were large unutilized funds and then the rug was pulled under our feet when the programme picked up momentum—notably by the US which reneged on its promises.

Personally, however, I gained much. Having to deal with 180 different countries widened my horizons and gave me many opportunities for useful visits, the visit to China being the most memorable. I also gained some insight into the realities of the rest of Asia, Africa, the Middle East, southern Europe and South America. Besides, I now had to be concerned not just with economic policy, but policy on health, education and so on. True, this widening and deepening of my experience was rather superficial—I could hardly stay with any country or problem for long. But I did learn a lot. Personally too, it was a very happy period, with much cultural exposure, many new friends, visits of artists from India who stayed and performed in our spacious house in Riverdale. Again, our daughter was growing up well; and we had some money for the first time in my life.

China

My first visit to China just before I left for India is noteworthy for many reasons. Despite the fact that I was leaving for India soon—

and, indeed, as it turned out, because I was leaving—the Chinese insisted that I should visit China to negotiate the first clutch of projects to be financed in China with UNDP assistance. During my stay of some twelve days, I was treated with the utmost courtesy, and at my request taken to such distant places as Tachai, Hangchaw and Shanghai in addition to Beijing. They even traced a Cambridge friend of mine, Tang Sheng, whom I had last seen in New York in 1948 just before the Communist take over. I was happy to see that she was none the worse for her three decades of service in the Chinese Ministry of External Affairs.

What impressed me most, however, was the fact that even in 1977—just after the liquidation of the Gang of Four and before the sharp turn in economic policy—it was obvious that China had abolished poverty of the kind that still blights India. Whatever the final verdict of history, the Chinese communists had at least one achievement: they created an entire nation of literate, reasonably well-fed and sheltered people. This is perhaps the main reason why the Chinese economic progress has been so spectacular after the adoption of the new liberal policies. The signs of China's willingness to learn and change and think of the future were also there. The three projects they wanted the UNDP to finance were (a) computerization (b) environmental protection and (c) framing of economic policy. And this was in 1977! I was questioned at length on the budget-making process, monetary policy, exchange rate management and the like. They had not insisted in vain on my going to China just before returning to India!

*Towards the RBI**

At home, the big event was the Emergency; and was I glad to be away. I could not have swallowed it. I am told Mrs Gandhi, during her first meeting with senior civil servants soon after declaring the Emergency, referred to my reaction (after Morarji's ouster) and asked them to follow my example: even if they did not agree

*London, 24 May 2000.

with her policies, they must faithfully implement the policies, as long as they were in the Government. I had no desire for an encore of her encomium. When my three years at the UNDP were completed at the end of 1975, C. Subramanian who had taken over as Finance Minister, asked me to return. I requested extension of my leave for two years which was granted.

When the Janata government came to power in 1977, I was asked to return as Governor, RBI. I had stopped by in Delhi on my way to Manila, and I asked to see Mrs Gandhi, Morarjibhai and H.M. Patel who had taken over as Finance Minister. Mrs Gandhi was the first to return my call. This meeting with her was most cordial and she seemed anxious, if not glad, to see me. I told her that she should write her memoirs. Her years as Prime Minister were an important part of our national history and the world was entitled to hear about them from herself. She pleaded lack of time and said she could hardly think clearly as long as the Janata government was after her blood. I said I could not believe Morarjibhai would be vindictive. She agreed, but said: 'There are all those monkeys around him. Since you are seeing him, please ask him to keep them under control.' Everyone has a human face.

Morarji came straight to the point after I mentioned my visit to Mrs Gandhi to which he merely responded: 'We cannot forget that she was the Prime Minister of India and the daughter of Nehru.' He said some people wanted me to return as Deputy Chairman of the Planning Commission. But his choice for that post was Lakdawala. He wanted me to go to the Reserve Bank. I agreed but requested that I be allowed to take charge in December when I complete five years at the UNDP and become entitled to a pension. He readily agreed that I should not forgo the pension and that they would make temporary arrangements.

H.M. Patel repeated the offer and could not understand why I was so keen on a pension and not joining immediately. But I had Morarji's support, and M. Narasimham was made the Governor to keep the seat warm for me. That summer, Morarji was visiting London and I went to see him from Geneva where I had my Governing Council meeting. Among other things I suggested that R.K. Hazari should not be disturbed as Deputy Governor of RBI. I

knew that he had been openly and even viciously critical of Morarji. But he was an able economist and I knew I could get along with him. There was no point in allowing the past to cloud the future. But Morarji was indignant. He said I had no idea how much harm Hazari had done to him and that if I thought he was a good man, my judgement was questionable and he (Morarji) wondered if he had made a mistake in putting his trust in me. I replied immediately that nothing was lost yet and that he could reverse his decision. He immediately changed his tone and tried to mollify me.[1] On an earlier occasion, he had also asked me whether Manmohan could be trusted as he had been close to Mrs Gandhi during the Emergency. I had advised that Manmohan was not only very able but a man of integrity as well and would serve Morarji loyally.

In the autumn of 1977, I attended a party in the Fund atrium in Washington to celebrate, I believe, the seventieth birthday of E.M. Bernstein who was my boss in 1950–4. He was succeeded by J.J. Polak as Economic Counsellor and Polak too was due to retire soon. Both of them were very keen that I should succeed Polak as Economic Counsellor. Normally, I would have been greatly honoured to accept the position. But I had given my word to Morarji and they had waited for me. Besides, we did want to go back and work in India. Bernstein and his wife Edith were very fond of me. Years later when I had forgotten our conversation in 1977, he chided me that I had preferred the RBI job to being his successor, but added, 'And you were right, too. You were needed in India.' It was Bernstein who during 1950–4 had done his best to train me as an applied or policy economist and who had made no secret of the fact that he was training me for service in India. I am glad that I had not disappointed my mentor at least in this respect.

Endnote

1. I had another altercation with Morarji before taking over as RBI Governor. He wanted me to reduce interest rates when I took charge—to some 6 per cent. I had to tell him that that was neither possible nor desirable and that he would have to find another Governor if he was keen on it. I never heard about it again.

7

The Reserve Bank of India 1977–82

During my five years at the Reserve Bank, I had to deal with five Finance Ministers: H.M. Patel for about two years; Charan Singh for about six months; H.N. Bahuguna for nearly six months; R. Venkataraman for a year and a half; and Pranab Mukherjee for the last few months.* This record is sufficient indication of the fact that nothing approaching a systematic and coherent set of policies was pursued during the period. Basically, routine duties were performed and there was much posturing, but little planning or purpose. And yet, the period was interesting in many ways. I learnt for the first time how important it is to resist and say no, at least for the RBI Governor; and I have to say that if I have to claim any credit for myself as a Governor, it is largely in the tenacity with which I resisted pressures of the wrong kind. It had more to do with holding the fort than constructing new mansions or highways. In addition, of course, there were crises which add spice to any responsibility. I also greatly enjoyed the opportunities that a Governor has, to speak in the public on issues of importance—even those beyond Central Banking. Perhaps most important from the personal point of view were the opportunities to be a part of international discussions

*London, 24 May 2000.

and think-tanks. I was particularly lucky to be invited to be a member of some very rewarding groups in addition to opportunities that arose in the normal line of duty.

Janata Government: The First Flush

The Janata Government was careful enough to maintain continuity with the past for the most part. But it did feel obliged to pursue some half-baked ideas in keeping with its image of 'an alternative' in governance. There are always politicians who believe that one way to punish their corrupt predecessors is to demonetize high denomination currency notes. There were people in the Janata coalition who felt this way—and no one felt strongly enough to oppose them. Accordingly, H.M. Patel informed me that it had been decided to demonetize 1000 rupee notes. I pointed out that such an exercise seldom produces striking results. Most people who accept illegal gratification or are otherwise the recipients of black money do not keep their ill-gotten earnings in the form of currency for long. The idea that black money or wealth is held in the form of notes tucked away in suitcases or pillow-cases is naive. And in any case, even those who are caught napping—or waiting—will have a chance to convert the notes through paid agents as some provision has to be made to convert at par notes tendered in small amounts for which explanations cannot be reasonably sought. But the gesture had to be made, and produced much work and little gain.

Another measure for which I had little enthusiasm was the sale of gold officially to discourage smuggling. I tried to dissuade H.M. Patel from pursuing this path. But he obviously was under pressure and had to do something. To import gold on a scale large enough to make smuggling redundant was inconceivable in the strained circumstances of the time. Ultimately, I insisted that the RBI would undertake the selling of gold only as an agent of the Government and not on its own account. It would also not advise using our scarce foreign exchange reserves for the purpose of importing gold. This only left gold already owned by the

government by confiscating smuggled amounts earlier and the small output of Kolar. Such a limited enterprise could not produce much impact on smuggling and could not last long. Neither could it do much harm. All I can say is that we trimmed a half-baked and ill-advised policy enough to make it virtually harmless. It still left some tricky work for the RBI to perform: how to sell the limited amount periodically in a manner which was fair and objective and how to avoid information being leaked and avoid charges of corruption or favouritism. Care had to be taken to see that there was no cornering of the supplies while getting as high a price as possible. For the RBI this was an arduous and unenviable task.But I can claim that under the able leadership of M. Ramakrishnayya, a senior Deputy Governor and former Secretary in the Government of India, the job was done with every care and in a strictly professional manner.

It was impossible to avoid allegations in a politically surcharged atmosphere. Mrs Gandhi later instituted an inquiry by R.K. Puri, a former Governor of the RBI during the Emergency. He was reported to have been given charge of the RBI to ensure pliability. Asking him to enquire into the conduct of those who replaced him smacked of deciding on the verdict before starting the enquiry. But Puri could find nothing objectionable; and in fairness to him, I must say that in questioning me and my officers, he was scrupulously courteous and professional and not confrontational at all. Whatever may have been the truth about his stewardship of the RBI, his conduct of the enquiry was irreproachable as far as the Bank was concerned.

An important development during H.M. Patel's stewardship was the settlement of the long-outstanding problem of the rupee–rouble exchange rate.* A crucial part of Morarjibhai's policy was to continue what was valuable in earlier policies and not to undo things

*London, 27 May 2000.

merely for the sake of undoing, while taking fresh initiatives when needed. Thus planning was not downgraded, but given a new lease of life under Lakdawala. Relations with the Soviet Union were valued and strengthened—and the anxiety to settle the rupee–rouble problem was a part of this approach. At the same time, the hand of positive friendship was also most decisively extended not just to the US but to Pakistan as well. Relations with China were sought to be normalized. And there was a distinct warming up in our relations with the Bank and the Fund as well. The rupee–rouble ratio question was settled rather easily. By then, my friend Alkhimov had taken charge of the Central Bank in the Soviet Union; and Manamohan Singh as Economic Secretary and myself saw eye to eye on this issue as indeed on most issues. Alkhimov was invited to India and a solution was arrived at.

A difficulty arose when everything was ready for signature. Under Government of India rules, agreements on behalf of the Government could be signed by a Secretary to the Government, but not by the Governor of the RBI unless he was specially authorized by the President. Accordingly, we proposed that Manmohan Singh sign on our behalf. This was not acceptable to Alkhimov who had set his heart on signing it and would sign it only with his counterpart. The President was away and could not be contacted in time to allow the Russians to leave Delhi as planned. H.M. Patel suggested a way out. Two persons should sign from each side. It did not matter that one of the signatures on our side was redundant and indeed useless. Ministerial astuteness was vindicated, and the RBI Governor was put in his useless ornamental place!

It was during H.M. Patel's ministership that I was asked to consider granting a licence to the Bank for Credit and Commerce International Ltd (BCCI) to open a full-fledged branch in India. They already had a representative office. Our policy in regard to the opening of branches by foreign banks then was restrictive; and our scrutiny of the BCCI representative office had given us cause to suspect that their activities were not above board. Money-laundering was suspected. Besides, the fact that the Bank of England had not given it a licence while permitting it to operate also meant

that the BCCI needed at least more watching before a licence was given. My advice to reject their request was readily accepted by the Government. The BCCI then tried its best to sway my opinion—including an offer to start a world-class institution of economic research in honour of my father-in-law, A.K. Dasgupta. The offer was made through a Bangladeshi economist whom we both knew earlier in the Fund and who was now with the BCCI. The condition, of course, was that I should be associated with the Institute. I could only refuse the honour politely as I knew what lay behind it. But the BCCI had tried to gain respectability by setting up a Third World Institute and offering Third World Prizes with which persons like Sunny Ramphal and B.K. Nehru were innocently associated.

Charan Singh

Charan Singh was sought to be placated some time in 1979 by giving him the Finance Ministership. H.M. Patel was removed to Home. I was a bit apprehensive that Charan Singh might be a bit hostile to me because of my association with Morarji; and I had some support for this when in my first meeting with him as Finance Minister, he was aggressive and questioned my credentials as I knew nothing of rural India and of agriculture, in particular. I informed him of what the RBI was doing for the rural sector—and also incidentally, that the Patels were really the Jats of Gujarat. It has to be said that after this meeting, I was left alone and never asked to do anything which I thought was improper. My advice too was valued. And on one major issue, Charan Singh backed me fully.

From the start, I was bedevilled in the RBI by militant trade unionism. On my first visit to Calcutta, I was 'gheraoed'[1] and shouted at for hours. The issue then was 'no computerization'. We were only contemplating the computerization of the statistical department in Bombay but the unions were up in arms everywhere. The promise that there would be no retrenchment was not enough.

The argument was that as a national institution the RBI should set the pace in creating employment and should increase the size of its staff year-by-year. I had my way on computerization of the statistics department by making careful arrangements to have the new equipment installed overnight—the night before the unions organized a big crowd to prevent the computers from being delivered. They then took up the question of wages and salaries; and, I was able to secure the approval of the government to a generous package with great difficulty, mainly because Manu Shroff, the additional secretary in charge of Banking, was cooperative. But the unions were adamant and went on strike. I could persuade Charan Singh and Morarji to declare the RBI as an essential service and make the strike illegal. This was done despite some opposition, notably from H.M. Patel as Home Minister. We managed to bring the unions down to earth: all they wanted now was that the issue be resolved, with some little face-saver for them. Shroff and I had worked out such a formula and we were to meet the union leaders in Delhi to clinch the issue. But just at that time, the Morarji government fell; and the new Finance Minister, H.N. Bahuguna, was only too happy to pose as a progressive saviour of labour and gave them all they wanted.

My last encounter with Charan Singh—or first with him as PM—also left me with a good impression. I learnt that despite all that was on the file, a junior minister in the Finance Ministry had passed an order on the very last day of Morarji's government sanctioning a branch for the BCCI. Manmohan Singh who received the file was unhappy about this last-minute decision and informed me. I immediately contacted Charan Singh who, despite all that was on his mind, gave me an appointment at 5.30 a.m. next morning (I had said I would like to see him before I returned to Bombay that morning). I was ushered into his bedroom. I gave him the background of the case and requested that, despite the orders passed, the matter should be kept in abeyance till he as Prime Minister

had time to look into it. I offered to see him again whenever he wanted to. He simply said: 'Where is the question of my thinking further? You have explained everything. The licence will not be given. Tell Manmohan Singh to disregard the orders passed.' I relieved Manmohan of his anxiety and called on him at his residence on the way to the airport.

The brief period of Charan Singh's prime ministership was uneventful except for the fact that it showed Bahuguna in his true colours. I have had reasons to complain of undue pressures in Delhi in 1971–2, and from Delhi after 1980. Bahuguna was no different. I could disregard him only because I knew by then that I could take my case to Charan Singh.

The Return of Mrs Gandhi

Mrs Gandhi's triumphant return to power in 1980 certainly injected a new life in Indian politics but not so much in Indian economic policy. My impression is that Mrs Gandhi had by then lost any revolutionary fervour that she might have had, and did not need any radical crutches now. Her position was secure; and she was soon to be made aware that the second oil crisis had had such a severe impact on the Indian economy that we were already planning for a very large drawing on the IMF. What her return did bring in, however, were a new set of actors on the political scene who were all anxious to make their mark by hook or by crook. That meant more people to fend off for the Governor of the RBI.

My first brush with the new kids on the block occurred when I came up against the newly elected young Chief Minister of Maharashtra, A.R. Antulay, who had none too savoury a reputation for his part in the Emergency. His first step as Chief Minister was to announce that he would write off certain debts of farmers. In fact, this promise was first made by Sharad Pawar during the elections and I had opposed the idea publicly. For this, I was gheraoed by Pawar's supporters at the Aurangabad airport. I had no choice but to repeat my opposition when an incumbent Chief

Minister made a similar announcement. Antulay reacted publicly in style—so much so that R.K. Laxman was inspired to sketch a cartoon showing Antulay running away with, I think, Rs 40 crores and myself trying to catch him while remaining half behind a screen.

The dénouement of this episode says a great deal about the climate of the time. A junior minister in the Ministry of Finance, Maganbhai Barot, brought Antulay and myself face to face at his house, and Antulay asked me very politely how I could have any authority over an elected leader—a very legitimate question. I clarified that my opposition was to the proposal to use RBI money through NABARD to write off the loans. He was sharp enough to reply that in that case, he would use the state exchequer to fulfil his electoral promise. I said that while I could not prevent him from doing so, I was bound to advise him and the Union Finance Minister that this would set a very bad precedent and would not contribute to financial discipline. Antulay immediately suggested we all call on Venkataraman, the new Finance Minister, who knew me well and was very fond of me. But he had deserted Mrs Gandhi at one point and was insecure in his new post. He listened very carefully to both of us, said nothing, and just smiled. Antulay was known to be very close to Mrs Gandhi and Venkataraman wanted to take no chances by taking a firm position. Antulay naturally took this to be 'no objection' and went ahead.

There was so much comment and criticism of this step that at the forthcoming meeting of the National Development Council, several Chief Ministers referred to it. Mr. Venkataraman was obliged to say that what was done should not be repeated; and Sanat Mehta, the Finance Minister of Gujarat, sprang on his feet to enquire if what was meant was that each state can do it once and no more. In due course, writing off debts became an electoral gimmick and a periodic stab in the back of financial probity.

Such is the irony of life that one of the first steps I had to recommend to Mrs Gandhi was that she should nationalize another swathe of private banks. The Reserve Bank had the responsibility to supervise private banks and to ensure their compliance with social control norms as well as with law. Several small private

banks had now grown to respectable size and it was not easy to control their activities in practice. Some of them, like the Punjab and Sindh Bank and the Vijaya Bank, had become the personal fiefdoms of individuals who disregarded all rules and advice with impunity. They, with their shady dealings, were offering unfair competition to the nationalized banks. I decided that the only practical way to tackle the problem was to nationalize the banks which had now reached the cut-off point of the 1969 Act. Mrs Gandhi readily accepted the advice—going against her promise of no new wave of nationalization, strictly speaking. But it must be said that she had no appetite for nationalization now and that this particular initiative for the second phase of bank nationalization came entirely from me.

The non-banking financial institutions were equally a pain in the neck. Their practices were questionable, offered unfair competition to banks and they were often deceitful in dealing with their depositors. It was a moot point in what way they were non-banking: they did take deposits even if the depositors could not write cheques; and they did give credit, even if this did not take the form of opening chequeable accounts. The security of depositors was a real issue here just as much as sound credit policies. But RBI's control over these institutions was ineffective then, and remains so even now. The only control is through the arm of the ordinary law. This area still awaits satisfactory resolution.

Mrs Gandhi was also very supportive when I was confronted by yet another bout of labour trouble. The RBI union in Bombay was led by the Shiv Sena which was then reputed to have very close relations with Antulay. Emboldened by this and Mrs Gandhi's victory, the local union leaders started making all kinds of unreasonable demands, interrupting work, and gheraoing us. One of their demands was that each worker on retirement should be replaced by a relative. On one occasion when I was in Manipal attending a banking seminar, I was telephoned to be informed that several staff members had abandoned their posts leaving lakhs of rupees in cash unattended and at risk—a most serious breach of discipline. I advised immediate suspension of the whole lot and a departmental enquiry. The results of the enquiry were obvious. But I could not act without Mrs Gandhi's support. For one thing,

my officers and I were continually threatened; and I could not ask my officers to act firmly unless their safety was guaranteed. This meant support from the state government. Secondly, there would be no point in taking firm action if it was to be reversed later under political pressure. Mrs Gandhi listened to me carefully and at first asked rather sarcastically if I was once again proposing recourse to the Essential Services Act. I said no, but requested two things: that she speak to Antulay and ask him to give us police protection, and that she should not ask me to take back people whom I dismiss. She was true to her word. She never suggested that I take back any of the persons whom I dismissed; and Antulay helped in every way. In fact, Antulay remained helpful and friendly thereafter throughout my tenure and indeed afterwards whenever our paths crossed. In London, he called in at my LSE office to tell me how happy he was to see me there. He always referred to my wife as 'Bhabhiji' and helped in securing reasonable housing for some needy and deserving artists.

The Second Oil Crisis

By the latter part of 1980 it was clear that the second oil crisis had created a serious balance of payments problem which necessitated a large Fund drawing. We had already drawn to the hilt on the special oil-facility at very concessional rates. But much more was required. The Fund was also encouraging members to come to it at the early stages of difficulty rather than wait till a crisis was upon them. Our negotiations with the Fund were very successful and we were to get the largest drawing, to date of $5 billion SDRs. The conditionalities were not at all severe. We had to improve our budgetary position which was in any case necessary. For the first time in our history, we had a revenue deficit in 1980–1 and this was regarded then as unacceptable by all parties in India. The only other condition was that we had to improve our balance of payments position in the medium term by expediting the exploitation of the Bombay High reserves. Even for Mrs Gandhi, with her bitter experience of devaluation, this package was no anathema. At the Tidewater meeting in Kuwait, the new Managing Director,

Jacques de Larrosiere informed me that he was happy with the agreement we had made with the Fund team and that he would deliver as long as the budget for 1981–2 was in line with this agreement—which it was.

At the meeting of the Interim Committee in Gabon in May 1981, de Larrosiere changed his tune and said that he was not satisfied and needed further discussions. We were furious and made no secret of it. What had happened in the meanwhile was that President Reagan had taken charge and was opposing the Bank and the Fund on ideological grounds. He was being advised that the private banks could meet all legitimate needs of all countries, rich or poor, and that the Fund and the Bank were no longer needed. The US banks, led by Charles Wriston of Citibank, launched a special attack on the proposed drawing by India. I was, in earlier years, under great pressure from American and other banks to borrow on commercial terms more than we were willing to do. In particular, we refused to borrow for financing trade which had no risk for the banks and which we could finance with our reserves rather than by borrowing more expensively on commercial terms. We also used to make calculations about how much short-term commercial debt we could afford without straining our ability to meet our obligations on due dates. Our reputation in this regard was unimpeachable and we did not want to spoil our copybook by borrowing too much. The private foreign banks were peeved that they were losing out on what they thought was a low-risk opportunity for lending. Wriston had even evolved a theory of sovereign debt: that the debt of sovereign governments would always be honoured and had thus little or no risk. We did not fall for such facile reasoning and consequently became the target of pressure by US banks on the new US administration. The argument was that we were keen on IMF help only because it was cheaper and not because we needed it. The Fund was thus crowding out the private banks.

I called on Paul Volcker[2] whom I knew well and explained our position. My thesis was that given the Fund drawing, we would borrow even more from the private banks as our needs were large and the whole package would then be more manageable. In the absence of the Fund drawing, we would be obliged to borrow less from private banks and curtail our demand for imports as a large addition of expensive borrowing would be unmanageable. Volcker was very understanding and he tried, through Tony Soloman of the New York Federal Reserve, to soften the attitude of the US banks—to little avail, I am afraid.

We then launched a worldwide campaign to seek the support of all Fund members. We worked hard on de Larrosiere's French pride, reiterating that he could not let the US run the Fund and reminded him of his Tidewater remarks. He soon came round and batted for us particularly in France. We had good support in Germany where I knew many persons by now. I had also the full support of Geoffrey Howe of the UK whom I had met the year before in Malta at the Commonwealth Finance Ministers' Conference and with whom I had got on very well. Ultimately, the US was isolated as it had been in 1971 during the Bangladesh War, and it decided to abstain rather than vote against our drawing from the Fund. I had worked hard on this matter and we finally got our 5 billion SDRs and avoided a crisis.

There were some interesting sequels to this. The Planning Commission argued that the Budget should take credit for this drawing as it was a real resource and should go towards adding resources for the Plan. The Prime Minister was told that the old-fashioned Governor of the RBI was sticking to old-fashioned accounting conventions in this regard and thus inhibiting a reasonable plan size. I had to stand by my views. How the Fund drawing was accounted for in the Budget was simply a matter of accounting conventions to which we had adhered all through the years—and have subsequently. Fund drawings are not loans, but are purchases of foreign currency with Indian currency. The two balance out in budgetary terms and there is no net effect on the budget—as there is none when the Fund drawing is repaid. What happens in real terms when the additional foreign exchange reserves are drawn down is a different matter altogether. To show budgetary credit now for the Fund drawing would only make matters look

that much worse later when repayments are made. In the case of the oil facility, where we received a loan, the proceeds were taken into the Budget with a net favourable effect immediately as happened in every case of a loan. All I can say is that this was not the first time when special pleading was used to try and increase the size of the Plan in the short run while shutting an eye to the future. Happily, the accounting conventions were maintained, I should add, also because the Ministry of Finance was firmly behind me.

Having got the money, Mrs Gandhi was not keen on taking all the measures required for financial discipline and, in fact, decided to forego the last tranche of the drawing. The reason given was that we did not need the money. The real reason, I am sure, was that we were not prepared to pay the price. Drawing the full 5 billion SDRs would have certainly reduced the need to borrow from the market in the years to come.

Another echo of our drawing was heard in 1982 during the Toronto Bank–Fund meeting when the Mexican crisis broke and Volcker did not attend the meeting as he was busy collecting money to shore up a friendly country. The honest man that he is, he told me later that he thought of me then and that the contrast between the US attitude to India and to Mexico was striking. After all, the Mexican crisis proved us right—that there can be such a thing as too much borrowing from, and too much lending by, private banks, and that Wriston and his theory of sovereign debt were woefully wrong. Economics always overtakes cleverness in real life.

Managing the Exchange Rate

Since the collapse of the fixed exchange rate system in 1972, there has been a great deal of debate about a proper system of exchange rate management. After the 1966 devaluation, we persisted with linking the rupee to the dollar, albeit at a new rate. When continued inflation and balance of payments difficulties at home necessitated a further devaluation, we achieved this surreptitiously by linking the rupee to the weaker sterling rather than to the strong

and strengthening dollar. But such stratagems cannot help for long. For some years, we experimented with a link with a basket of currencies—and here too, we played around with altering the weights in the basket to accommodate the required degree of devaluation. But there were limits also to this kind of manipulation within a basket. It could not, for example, prevent an appreciation of the rupee in real terms in the early eighties when there was an upsurge in inflation after the second oil crisis. A formal devaluation was a non-starter in those days of fractious and fiercely competitive politics. Even the IMF did not insist on this at the time of the 1981 drawing. But the logic of the situation would sooner or later dictate an abandonment of the basket in favour of a floating rate—even if the float is managed to take care of speculative and other pressures; and this is the system we have followed now for many years with reasonable success.

But a 'managed float' is just a phrase. It does not tell us how or what to manage; and there are no simple rules one can lay down for this purpose. There are some modern mercantilist mandarins who would miss no opportunity of keeping the exchange rate undervalued in real terms and who would like to add to foreign exchange reserves at all times. But if everybody works towards an undervalued rate, we would soon revert to the chaos of the inter-war years. We export because we want to import as much as possible and as cheaply as possible. Once tariffs are low and import restrictions are virtually abolished, the only way of reaping the benefits of good export performance is to appreciate and make imports cheaper: there is no sense in piling up reserves for ever. If the upward pressure on the rate is the result of temporary factors like large but reversible flows of external capital or a sudden and sharp but reversible increase in export prices, it would certainly make sense to support the dollar and build up reserves; but this would raise its own questions of how much of this acquisition should be sterilized and how.

To tread the middle path and keep the real exchange rate stable is neither easy to implement nor always right. The calculation of the real exchange rate, when 20 odd countries compete with us

equally at the margin in our export markets (and a different set for each export and yet another set if we think of competition in our own market), is at best an intelligent approximation. A managed float thus is not a simple or a well-defined proposition. And in these days of free international movement of capital, we know that national authorities have not got all the degrees of freedom.

In the ultimate analysis, no management by economic instruments alone can deliver us from basic or fundamental infirmities such as a low rate of savings or an inefficient use of the savings and, generally, low productivity all round. These have to be dealt with on their own terms by a combination of economic, social and political steps which take time to gain hold and yield results. There are no antibiotics available yet for economic health. Surgeries like currency reform or a large devaluation or restructuring the debt of governments, banks or big corporations may sometimes be necessary. But frequent surgeries can be fatal. Lasting economic health requires good sustenance (education, training and a healthy environment), an active life (hard work, competition, enterprise, innovation and even animal spirits), a disciplined and moderate temperament (good governance, rule of law, respect for law, willingness to cooperate and perform civic duties, and refraining from destructive agitation) and a proper balance between today and tomorrow (savings, sound fiscal and monetary policies and care of natural resources and environment). Economics is not just a part of life. It is as large as life itself.

Credit Policy

For the reasons mentioned earlier, my tenure at the Reserve Bank cannot be credited with any significant departure in monetary policy. We did conscientiously formulate the seasonal credit policy, taking into account the needs of the economy as best as we could. In such matters, fine tuning is not possible; and the tendency to claim credit or apportion blame with hindsight for how fine or otherwise the tuning was, however inevitable and understandable, has little to do with how wise or otherwise the original steps were.

All I can say is that nothing sensational was attributed to RBI policies at that time.

One incident, however, is worth mentioning. As part of a periodic review of credit policy, I had on one occasion reduced the cash–credit ratio for banks by 0.25 per cent to enable the banks to meet the legitimate needs of the public and the private sector as we saw them. This released some Rs 500 crores to the banks for further lending. After all, credit policy was not always to be tightened; it could be relaxed also; and the CRR was not a mechanism for raising money for the Budget. But at a meeting of the Planning Commission where the Prime Minister and Finance Minister were present, this step was criticized and it was alleged that I had gifted Rs 500 crores to the private sector at a time when the government was finding it difficult to raise resources for the Plan.

The Economic Secretary, Ram Malhotra, told me later that the Prime Minister had asked for the Ministry's explanation. He had explained the position; but she was not satisfied, and he asked me to see the Prime Minister's Secretary, P.C. Alexander. I saw him and explained the rationale for my action, and the point that more than half the additional credit was intended for the public sector, especially oil, so that the charge of favouring the private sector was patently absurd. I could understand the argument that the credit situation was not such as to require relaxation. These are matters of judgement. But to say that I helped the private sector was a loaded statement. Eventually, I was asked to explain my action in writing, the only time in my long career that I was asked to do so.

Needless to say, under these circumstances, I could not have my way even in running the Bank. Before the arrival of Mrs. Gandhi, I had no interference in the appointment of my senior staff. The choice of Ramkrishnayya as Deputy Governor was mine and approved by H.M. Patel wholeheartedly. The same was the case with Waman Tambe whom I brought from the Ministry as Executive Director. But I could not make him a Deputy Governor later as I wanted to, and he left for the World Bank. My attempt to invite Manu Shroff to become a Deputy Governor met with

the same fate. On the other hand, I had to work hard to avoid having a Deputy Governor who I knew would be unsuitable. My view finally prevailed; but I had to suggest three names, of whom the one chosen was not my first choice.

*The Spoils of Power**

I had more than my share of undue pressure from Delhi after Mrs Gandhi's return to power. Some of the baggage she acquired after the Congress split and the Emergency was, to say the least, drawn from the bottom of the political drawer; and being asked to facilitate various shady deals, some of them were not averse to coming up with a few of their own. Thus, the Speaker of the newly elected Parliament, no less, was anxious that I should give a licence to a bank of his choice to open a branch in the newly opened Nehru Centre in Delhi. This was against our policy as it was then, and I told him so on more than one occasion. He must have also plagued Venkataraman who asked me to call on the Speaker, which I did in his Chambers in the Parliament House. I was asked point-blank whether the Speaker of the House was to be disregarded in a matter like this. I could not retort and ask what business it was of the Speaker to interest himself in a matter like this. But he could not get his way; and he did not forgive me for that.

Janardan Pujari and Abdul Ghani Chaudhuri thought nothing of picking up the phone to ask RBI officials to do various things—mainly instruct banks to give loans to some party or for some mela where a particular group of voters had to be obliged. I have to admit that my intransigence could not have hindered them much as it was quite easy to bypass me and get things done by my juniors without my knowledge. Thus, as was to come out in the House years later, a prominent Congress leader got a licence to open a personal foreign exchange account abroad during my tenure as Governor. My daughter asked me how I could have done that. Fortunately, she was old enough by then to accept

*London, 28 May 2000.

the explanation that I knew nothing of it. Some junior officer had obviously obliged. For all I know, there was some legal cover for it, however slender, as our regulations were full of loopholes.

The most persistent and obnoxious pressure, however, was on behalf of touts who wanted to offer us loans at rates more favourable than those that prevailed in the market. They all claimed to have special access to some Arab or Iranian money and were in a position to lend it cheap, albeit for a consideration. I could easily decipher their game: either they were frauds and we would not see the money once the commission was paid or they were out to launder black-or drug money. I would have nothing to do with them and refused to see them as they would exploit even such a meeting by name-dropping in future. I had explained all this to Mrs Gandhi and to Venkataraman. How would an honest man get hold of funds at a price cheaper than what the banks would offer? If I remember right, some officers from Delhi were sent to Europe to make enquiries and had come back with similar doubts. Venkataraman agreed with me, but could not withstand repeated onslaughts. There were the usual accusations that the Governor and the Minister were old-fashioned.

Ultimately, I agreed to meet one of them at Venkataraman's house in Delhi. I had worked out a plan. I knew the Governor of the Central Bank of Switzerland, Fritz Leuitwiler, very well and had got from him the assurance that within an hour or so, he could tell me whether it was safe to receive money from—or pay it into—a particular Swiss bank account. I asked our visitor if he would tell me from which account in Switzerland he would transfer the money to us and in which account he would like his commission to be paid. I made it clear that I needed this information before I could make up my mind on how to advise the Government. I had always insisted that any such borrowing will have to be by the Government and not the RBI As soon as I made my point, our visitor got angry, said I had no idea of how the real world worked and stormed out of the room. That ended this particular chapter.

The BCCI chapter, however, was reopened, and this time with very powerful advocates. My position remained the same. A month or two before I was to leave the RBI, I got a call from the bank's representative in Bombay, requesting a a meeting between me and Abedi, the Pakistani chairman of the BCCI and its inspiration, creator and steerer. I agreed to meet him. The day before our meeting, however, I was informed that the meeting was off, that Abedi was not coming to Bombay as the purpose for which he wanted to see me was already served during his stay in Delhi! Obviously, he was told that I was leaving soon and that all will be well afterwards. And it was.

Leaving the RBI

By the middle of 1982, it was clear to me that Mrs Gandhi would be happy to see me go. I had no hope or expectation, or indeed any particular desire, to have a second term and was quite prepared to leave at the end of my term. But I saw no reason to leave earlier unless I was asked, which I knew would not happen. It was only that life would become increasingly difficult, and it did. By the time of the Bank-Fund meeting in Toronto that autumn, Pranab Mukherjee had taken over as Finance Minister. I knew that was my last Bank-Fund meeting and took leave of my old friends and colleagues and some of the new friends I had made. At the Tidewater meeting at the end of the Bank-Fund meeting, I did some plain talking about the aid scene and the dominance of the rich in the governance of the multilateral financial institutions. I was not sure if I would get another chance.

On the way back from that meeting, Pranab Mukherjee and I travelled together. He was very friendly—after all, I was a son-in-law of Bengal! He asked me what I would like to do after the RBI and rather unthinkingly I said that returning to the Fund would not be bad. He took this seriously, and later I was sounded out on whether I would go to the Fund as Executive Director. I had no intention of being under Mrs Gandhi's obligation and quickly sent word of my lack of interest. Mukherjee also made a rather tactless remark to me during that journey—that he was now closest to Mrs Gandhi as she had asked him to preside at Cabinet meetings in her absence from India. I knew that if Mrs Gandhi came to know of what her Finance Minister was thinking—and she had a way of knowing such things—that would be the end of the Minister's dreams.

I had one more bout of trade union trouble, this time from Calcutta where the union led by the very able and dour Ashish Sen decided that they would not close the books in Calcutta in time for us to be ready to close the accounts of the Bank, on the appointed day. This had never happened before in the history of the Bank and it would have been very embarrassing for me if I had to leave the Bank with this stigma. Our only way out was to remove the books from the Calcutta office and have them closed elsewhere. But this could not be done without state police protection. I had to call on Jyoti Basu and ask him to provide such protection. He was in a dilemma: he did not want adverse publicity, but was reluctant to humiliate a union leader of his own party. But he promised me support.

A few days later, Ashish Sen sent word to me that we should hand over the books to them and they would complete the accounts. He added that he respected me and did not want me to leave the Bank with a black mark. I had a difficult decision to make: if I let them have access to the books and they removed them, I would be in serious trouble. On the other hand, not to trust them would be an insult which they would not easily stomach. The books were given to them and honour was saved on all sides. Obviously, Jyoti Babu had leaned on Sen to do the right thing—and he did it graciously.

It was known that I was ready for another job and Manu Shroff suggested, at the instance of the outgoing Director, Vijay Vyas, that I might be interested in the directorship of the Indian Institute of Management in Ahmedabad. I readily accepted the suggestion which was welcomed by the Chairman of the Institute, K.C. Mahindra. Pranab Babu did the needful and Mrs Gandhi gave her approval to my appointment as Director, IIM. As their term had

already started, they were anxious that I join as early as possible and not wait till December when my five years as Governor would come to an end. Mrs Gandhi was only too happy to agree to this, and it was decided that the short-fall of a month or two would be disregarded for the purposes of Provident Fund and the like.

Once again, I gave a grand party to all the staff, including class four, in the gardens of the Governor's residence on Carmichael Road. This too was unprecedented and scores of class four staff—and others—came in bus-loads and inspected the whole house, as it was after all, the house of 'their Governor'. The warmth of their feeling and of that occasion was enough to convince me that I will continue to have their regard and affection even after I left the Bank—which, indeed, has been abundantly the case.

A year or so after I left the Bank, I arrived very late one night at the Delhi airport on my way to London.* I was very tired and was finding it difficult to ferry my heavily loaded trolley to the international terminal. Suddenly I found Mahadik, the leader of the Shiv Sena union whom I had dismissed and who had now become a Rajya Sabha member, approaching me with a smile. His plane also was delayed and he was very tired. But he would not let 'his Governor' push the trolley. He took charge of everything, got me seated comfortably and arranged with the Air India staff, a night's halt for me at Centaur Hotel so that I could rest and take the next morning's flight instead of the earlier one on which I was to travel. I was deeply touched.[3] The leaders of the officers' union—Nair and Kelkar—have kept in touch with me all these years. Even as late as the year 2000, all the unions in the Ahmedabad office jointly invited me to be the Chief Guest at their annual function honouring meritorious students during which many things about my tenure were recalled, which I had all but forgotten. Only Ashish Sen, who also became a CPI-M Rajya Sabha member, dropped off from my life.

*London, 29 May 2000.

Recalling Some Highlights

Despite the vexations of the last two years, the five years at the RBI were, on the whole, happy and enjoyable. The RBI Governor travels all over India and is received by dignitaries of all kinds. He also has occasion to preside over a variety of functions and make speeches, and he meets all foreign dignitaries visiting Bombay. I enjoyed all these occasions and learnt a great deal from them. Among visiting dignitaries from abroad, Sir Gordon Richardson, the Governor of the Bank of England, and his wife were my guests as also were Alkhimov and his party. The Prime Ministers of Uganda, Mauritius and others were entertained at the RBI. And on two occasions, I sat next to Margaret Thatcher when she visited India as Prime Minister. I had a long chat with her, and was impressed by her candour. At a lunch where she was pleading for joint Indo–UK collaboration in economic matters, she said very characteristically that while she believed in free trade, she would protect Indo–UK joint ventures from any unfair competition and that she would ensure them a level playing field. She knew how to play to the gallery.

Among Indian Chief Ministers, I found Jyoti Basu, Ramakrishna Hegde and V.P. Singh well informed and good company. But only Jyoti Basu was totally in command. I have already mentioned how he diffused the 'account books' crisis. On an earlier occasion, he was the only one who found a practical answer to a problem we had in many state capitals where we had offices. Either we had no land on which to build houses for our staff or the land we had was encroached upon. Most Chief Ministers, including Sheikh Abdulla, promised much and did nothing. Only Jyoti Basu told me honestly that even he could not evict the people who had occupied our land. Instead he gave us plenty of land in the newly developing Salt Lake area which served our purpose.

I gave many talks and enjoyed this part of my duty. My friend and colleague, V.B. Kadam, put all of these together in three or four volumes and presented them to me on my departure. He had every right to be partial to these speeches as they had all received his most incisive comments and criticisms before I finalized them. Most of the speeches, however, were extempore and the one I

remember most was on the occasion of a reception to a delegation from the UK after Mrs Thatcher came to power. I had fun telling them that it was rather short-sighted to look for friends and allies in India while shutting off one tap from which a lot of goodwill had flowed between the two countries over the years, viz., the steady stream of Indian students being trained in British Universities. After Mrs Thatcher raised the fees for foreign students, this stream was bound to dry up to a trickle.

Of the many visits abroad, the one to the Soviet Union was perhaps the most memorable. Alkhimov invited me to visit the USSR, and I went there with three of my colleagues from the RBI. We were treated royally and taken to Tashkent, Bukhara, Samarkand, Leningrad and, of course, Moscow. I am afraid it was clear even in 1982 that Russia had lost the economic war.

The Bank of England kept up one memory of the Sterling Area. The old Sterling Area countries were invited to London for initial 'discussions' first before the annual meeting of the Bank for International Settlement in Basle—which took place during the most agreeable summer months. Some of us—though not members of the BIS—traditionally went with the Bank of England delegation to Basle. No real business was transacted either in London or in Basle. But we had several superb lunches and dinners and we met and came to know people who mattered in the financial world.

The Central Banking community is a very close-knit and discreet community. But it is also bound by informal but strong ties of mutual loyalty and support. I greatly enjoyed this experience and the friendships made have been useful on many occasions. Paul Volcker as Chairman of the US Federal Reserve ran his own informal club of select Central Bankers. It had only four members—apart from him, the Central Bank Governors of Mexico, Switzerland and India. We met once a year for several hours soon after the annual Bank-Fund meeting in some quiet place.

The spirit of Central Bank co-operation was not absent in Asia either. Here existed a club of South-east Asian Central Banks which ran training courses and was in charge of managing the Asian Clearing Union. The union was more face than substance; but it provided an annual occasion for Central Bank Governors from Tehran to Djakarta to meet, discuss things of common interest and to do some sight-seeing on the side. We had several such meetings in India, Malaysia, Sri Lanka, Nepal and Djakarta. To the best of my knowledge, this was the only significant forum where Iran, Afghanistan, Pakistan, India, Nepal, Sri Lanka, Burma, Singapore, Malaysia, Thailand and Indonesia met—a forum which transcended many political and strategic differences. Our exclusion in the South-east Asian region has become even more prominent since then. I hope this forum is revived as it is a vital link in Asian peace and cooperation.

In the same spirit, I visited Bhutan to facilitate the setting up of their own Central Bank. Till then, the State Bank of India was the banker of the Government of Bhutan. But this could not continue: an independent member of the IMF was bound sooner or later to have a Central Bank of its own. It was best to achieve this smoothly and without rancour—and this was done. In the same spirit, as Economic Secretary, I had arranged for Sri Lanka and Bangladesh to join our constituency on the Board of the Fund and the Bank. For a long time, we could elect our own Executive Director on the Boards of the Bank and the Fund. But as our relative share in Fund quotas declined—we were laggards both in growth and trade—and as quotas were revised periodically, we lost this prerogative and had to seek the support of other members. Nepal was not inclined to join us: it felt safer with a South-east Asian group. Even Sri Lanka was not with us. To lose even Bangladesh and have to seek support in Europe or Africa or South America would have underlined the suspicions of our neighbours sharply. I proposed that we be generous and promise Sri Lanka and Bangladesh that they would always have their representatives as Alternate Executive Directors on the Boards of the Fund and the Bank respectively while we would retain the directorship. This way, they would benefit more than in any other grouping and we would get long-term security and lose only two posts for our officers for all time rather than from time to time. I was able to push this through our bureaucracy and the Sri Lankans and Bangladeshis

happily joined us—and have been happy with the arrangement ever since. Later, Bhutan joined our group.

From my UNDP days, I was a member of another international club called the Tidewater group. It was, I think, set up by Ed Martin, Chairman of the Development Advisory Committee of the OECD and consisted initially of the chairman, ministers in charge of aid in the OECD countries and the representatives of the Bank and the UNDP. The first meeting took place in Tidewater in the US. I became a member first as a representative of the UNDP. My presence at some of these meetings became embarrassing: they would discuss their strategies as donors vis-à-vis recipients. I felt obliged to leave the room. Later I argued that some representatives of the developing countries as well as of the oil producers should be invited to such meetings if any meaningful dialogue was intended. If any group wanted to meet separately, there were many other opportunities. This was accepted. I attended for many years as 'a recipient'—perhaps the only case in history where a 'donor' graduated as 'a recipient'! The oil producing countries were also invited after a while when they became 'donors'.

An even more interesting international forum was the Group of 30 of which I was made a member from its inception and continued to be so from my RBI days to the end of my period in LSE, that is, for more than ten years. Like so many other things, the initiative came, I believe, from the Rockfeller Foundation. It was felt that there were many forums where academics met, or financiers met, or multinationals met or government policy makers met. But there was no forum where all these actors and thinkers met together. In the new environment where private financial markets were becoming increasingly important and multinationals were spreading fast, it was necessary to have meetings between them and public policy-makers in an informal but informed setting. The academics would ensure outside expertise as well as a resource for further research where it was needed. Initially, Johannes

Witteveen, who had just finished his term as Managing Director of the IMF, was invited to chair the Group. It had very influential and distinguished members from the 'four constituencies' that made up the international economic and financial world.

We met once or twice a year in different parts of the world and discussed a variety of issues related to current financial developments and future plans, often on the basis of papers specially prepared or after a more detailed discussion in smaller groups. The first fascinating idea to be discussed was that of a substitution account in the Fund on which Witteveen and I worked. The US had an unfair advantage in so far as the role of the dollar as an international currency made the US immune from having to take remedial measures when it was incurring a payments deficit. This asymmetrical situation meant that the rest of the world had to finance a US deficit over an indefinite period and transfer resources to it. This system was as unfair or unjust as it was conducive to continued payments deficits in the world.[4] This state of affairs could be ended if all dollar reserves were replaced by a specially created international reserve asset and the Fund ran a separate substitution account governing the use of the reserve asset created for this purpose. Thereafter, the dollar would no longer be used as a reserve asset and the US, like everyone else, would have to meet its deficit by using its gold, foreign exchange reserves or its allocation of normal SDRs or by drawing on the Fund. This would be fair and constructive and work towards a sounder financial system in which the Fund would have a central role. The US would also be more willing to agree to the creation of normal SDRs from time to time. Needless to say, such a scheme had no chance of acceptance by the US.

With the advent of the second oil crisis, attention shifted to devices for stabilizing the price of oil. The Saudi Oil Minister, Yamani[5] was an active member of our Group, and a kind of commodity stabilization scheme was worked out. But once again, this was unacceptable to one side or the other depending on whether oil prices were rising or falling. Nor was it easy to agree on a 'fair' price for oil and on suitable indexation. The Mexican crisis brought

its own crop of studies and discussions. The Group's more successful endeavours were in less ambitious projects like bank regulation and improvements in settlement procedures, information sharing and the like. The continued US boom provided interesting differences of opinion about when the bubble might burst and whether the US would make a soft or a hard landing from its high-flying deficit.

It was during this period that I also attended my first meeting of the Interaction Council organized by Bradford Morse of the UNDP. This was a group of retired Heads of State who met once a year under the leadership of Chancellor Helmut Schmidt. Not having a retired Prime Minister from India who could be invited, they had once invited Swaran Singh. For some reason—perhaps because of my UNDP days and RBI connection—I was invited on a few occasions, either as a member of an expert group that prepared studies or at the meeting of the former Heads of State where the papers were discussed. On the three or four meetings I attended over the years, I met a kindred soul in Pierre Trudeau who joined me in taking 'non-establishment' positions. Helmut Schmidt was very forceful but listened carefully and was anxious to know why we thought as we did. One bee in his bonnet was that the Islamic states were the next danger to world peace and prosperity after the collapse of the Soviet Union. It was left to me to argue against this thesis which has become more popular since. My point was—and is—that the Islamic world is divided and that the fundamentalist forces in Islam were a danger first and foremost to the Islamic societies themselves so that they would remain internally divided and unstable till they cease to be extremist and return to the mainstream.

An Independent RBI?

Before ending this account of my days at the RBI, I would like to say a few words on the question of the independence of the Reserve Bank. I have always held that in a democracy, the Central Bank cannot be totally independent of the government of the day and that the elected representatives have to have an edge. But this does not mean that the Bank has to be as subservient as it is today. A fundamental change is urgently needed. Thus, I agree that the Governor has to be appointed by the Government. No group of wise men can be given this responsibility. But more can be done to ensure a good choice, more acceptable to the majority of parties and more immune to narrow political or personal pressures. There could be broad qualifications laid down by Parliament and the approval of an appropriate Parliamentary Committee be made mandatory. If a Government servant is chosen, he should resign from Government service and not return to it. To the best of my knowledge, I am the only one to resign from a government position on assumption of office as Governor, and I did not return to government service or to an office of profit in government. This should be made compulsory. I think the Governor should also have only one term of a fixed number of years, preferably six or seven. There would be no temptation to curry favour for renewal; nor would the Government be able to make short-term appointments or remove incumbents at will except in the event of gross misconduct after inquiry.

Once chosen, the Governor should be free to organize the work of the Bank as best as he sees fit. There should be no question of Government interference in the appointment of Deputy Governors and senior officers and in conditions of service and the like. Above all, the Governor should be free to take all disciplinary actions within the law. I found it most galling that the most outrageous actions of unions were condoned at the behest of Governments which were interested in the support of all-India unions. Thus, while I was not asked to take back the dismissed RBI staff, they were all reinstated as soon as my back was turned. In such a state of affairs, no organization can function efficiently.

Independence in matters of policy is a difficult matter, and I do believe that the Central Bank cannot be totally independent even in matters which fall strictly within the purview of monetary policy. The Central Bank Governor is not directly answerable to the Parliament and should not be. The Finance Minister has no

choice. He must then have the right to be consulted on important matters such as major changes in the exchange rate. In fact, such a decision must require an agreement of the Government as a whole. When exchange rates are fluctuating, day-to-day interventions are in the domain of the Central Bank, but correcting major trends or not correcting them should involve the Ministry of Finance. I would argue that changes in reserve requirements and in interest rates are essentially the responsibility of the Bank and the Government should not look upon reserve requirements as a captive support for its borrowing programme. Nor should it want interest rates kept low to subsidize its borrowing. But even here, I should think periodic consultations between Bombay and Delhi should be a norm. If the Governor is to be left free in this regard, the Finance Minister should have the right to say on occasion that he does not agree with his Honorable Friend in Bombay.

The reasons why the Central Bank cannot have complete freedom in monetary matters are two: it is not easy to define in operational terms what are monetary matters; and second, economic policy is about dealing with events as they unfold so that one cannot always be sure what should be done and when and in what amount. Also, there are several objectives and the desirable mix can change from time to time. The case of the Supreme Court is different: the judges have to defend the Constitution which is a carefully drafted explicit document in which much thought and participation has been invested. The Government of the day cannot be given the right to interfere in the interpretation of the Constitution. But what would be the equivalent of a constitution in monetary policy? To say that the Reserve Bank should be given the exclusive responsibility for price stability is facile. Price stability cannot be absolute at all times. Nor can it be achieved by monetary policy instruments alone. Mutual discussion and consensus are important here even though some areas like interest rates and reserve requirements or open market operations are left ultimately to the RBI.

One could also try laying down rules with Parliamentary approval, such as: no support to the Government budget by support to borrowing over a period. This might ensure better financial

discipline; although sometimes I suspect it will only lead to a different adjustment to government profligacy of the same order. If the borrowing is allowed to be monetized, we would have inflation and a balance of payments deficit which will lead sooner or later to a crisis and require remedial measures at least for some time before people forget the past. Alternatively, if the deficit is not allowed to be monetized, it leads to high rates of interest, low investment and low growth or stagnation which too bring about some sort of adjustment, perhaps more durable and more debilitating. Which one is better? Ultimately, only good sense on the part of the Government can lead to desirable changes; and this requires an alert and informed public opinion which demands discipline and accepts temporary hardship and sees through empty promises of politicians.

Epilogue

It is now more than 18 years since I left the RBI. Much has happened in the meanwhile and economic policy everywhere has seen a sea change.[6] But it would be a mistake to think that we have reached a safe, secure and well defined haven in our economic sojourn. I am afraid the journey will last for ever. There never was a Golden Age and never will be. Men will crave and cringe and crib and quibble and quarrel and create new problems. They will also soar and dream and hanker after a more harmonious, just and freer set of social, economic and political relations. There will always be debates and discussions on the moral, political, social and economic responses necessary to new challenges and new opportunities. And therein lies the thrill and the adventure. Utopias would be as dull as death. Economics at the end of the day is about choice; and the right, ability and desire to choose—which includes choosing something difficult, not yet there, and working for it—is what distinguishes us from the rest of creation. So let us economists rejoice that economic policy is forever; not any particular policy to be sure, but the search for a better one. The good will never be enough; and the best is a contradiction in terms.

Endnotes

1. Surrounded on all sides by an intimidating crowd which immobilized you. Yet another word which shows how much more economical—and elegant—Indian languages are in comparison to English!
2. Chairman of the US federal Reserve in the eighties.
3. I cannot resist quoting another rather amusing example of the respect in which RBI Governors are held by the RBI staff. During my first meeting in Calcutta in 1978 with the leader of the class four union, I was suddenly asked to come to the middle of the room and stand up. I did not know what was happening, but obliged. My interlocutor looked me up good and proper and pronounced: 'Good. The RBI Governor should have a good personality. He symbolizes the dignity of the Bank.'
4. With capital account convertibility, it was possible for funds to move from the dollar to other reserve currencies, and this would exercise some discipline on the dollar. With fluctuating exchange rates, this discipline will be exercised through a depreciation of the dollar and not so much by a drain on US official reserves. But the system, in a way, has become more symmetrical now.
5. The most highly regarded Saudi Minister of Oil in the eighties.
6. Some of my writings since the early eighties have been brought together in a volume entitled *Economic Reform and Global Change*, Macmillan India, 1998, reprinted in 1999.

Appendix I

The Long Shadow of the Second World War

The assertion in Chapter 1 that World War II cast a long shadow on post-war economic policy needs, perhaps, some elaboration.

The most significant impact of the war was felt on people's attitude towards inflation. For most of India's middle-class, long accustomed to the blessings of stable or declining prices, the experience of a very rapid increase in prices was truly traumatic. What they looked for after the war was a roll-back of the price-rise. Indeed, the political members of India's first Planning Commission wanted that to be an explicit objective of the Plan. The economists had a hard time explaining why this was easier said than done. When pressed on one occasion, J.J. Anjaria, the Chief Economic Advisor to the Government, replied in desperation that the only way to roll back prices to their pre-war level was to bring about a depression of the 1929–33 magnitude. And one member of the Commission interjected: 'Then why do we not have a depression!' The understanding about inflation a la C.N. Vakil—that it is caused by a disproportionate increase in money supply—also has continued appeal. The preoccupation with 'deficit financing' underlines this.

The war also brought with it our first exposure to controls and high, even extortionate, rates of taxation. They brought in their

wake widespread evasion and systematic strategies for getting around rules and regulations. The bureaucracy—no leftist institution—was largely in favour of these controls and high-taxes. Civil servants like A.D. Gorwala continued their campaign for rationing and attendant controls long after the end of the War. Public opinion on controls and high taxes was divided; and there was some ambivalence in the general attitude towards them. What is not in doubt, however, is the fact that most of these attitudes and ambivalence survived the war. The distrust of traders and industrialists as generally dishonest and extortionate was fertile ground for advocates of state intervention and ownership. This distrust has existed side by side with antipathy to controls and acceptance of their avoidance. The desire to tax the rich has not come in the way of widespread acceptance of evasion which continues to plague us. The superstructure of controls, once built up, was difficult to dismantle and could be easily restored and built upon.

The war was naturally a period of great scarcity, aggravated by the difficulties of international commerce. For many people, the moral was that India should be as self-sufficient as it can be—not just in industry, but agriculture as well. That international trade cannot always be relied upon in an uncertain and conflict-ridden world was a perception that came to be widely shared.

In their own way, Japan and the Soviet Union impressed the Indian middle class and spurred their ambitions for a resurgent India marching boldly and swiftly towards its rightful place under the sun. If Japan can do it, why not us? After all, our steel industry till 1935 or so was at least as efficient as Japan's if not more. It was not the Soviet ideology of communism, but the heroic defence of Stalingrad that warmed our hearts and made us feel that there was something in Soviet practices such as the institution of Five Year Plans that we could profitably emulate. The Bombay Plan was drawn up during the war largely by industrialists; and in its boldness and sweep, it heralded what Mahalanobis and others were to try to advocate later—essentially, a short-cut to a strong and prosperous industrialized India through a heightening of national purpose, confidence and solidarity.

In short, the post-war preference for price-stability vs. growth, management and planning vs. free markets, closed economy vs. freer international trade, public sector as against private enterprise, and the on-again/off-again flirtation with controls and high taxes all had some roots in our war-time experience.

The war also saw the beginning of a new era of economic management and international economic cooperation. If part of the explanation for the war lay in the economic chaos and suffering of the inter-war years, something had to be done both nationally and internationally to avoid a repetition of such chaos and suffering. Nationally, this meant deliberate economic management and some redistribution. Internationally, attempts were afoot at setting up global economic institutions which would lay down common rules of national behaviour and international cooperation. India was an active participant in these international discussions; and the idea of managed economies with some redistribution also fell on willing ears here. The desire for social harmony and peace between groups and nations, even more than that for economic efficiency, provided the inspiration to the common man in his support for a new era of economic management both in India and the rest of the world.

Appendix II

On a Personal Note

It has been suggested that I have been rather reticent in one respect. Having worked with so many leaders of strong and differing persuasions, often antagonistic to each other, it could not have been easy to retain their trust. Would it not be of interest to at least some of the readers if I were to comment on this aspect of my experience?

The short answer to this question is that, by and large, I retained the trust and, in some cases, even the affection, of all the leaders I worked with; and I developed respect and regard for most of them. Despite several awkward moments, this is true even of Mrs Gandhi. She could not shed the suspicion that I was a 'Morarji man', and perhaps she was incapable of accepting that anyone could be his own man. But we worked well together in 1966–72; and even during 1980–2, I received good support from her regarding some difficult problems in the Reserve Bank. I knew she would not force me to do what I did not want to do. I had—and have—serious reservations about her political style and about the corrupt coterie that grew around her and about the long-term impact of all these on Indian life. But I had no real quarrel with her economic policies and have had respect for her patriotism, courage, and ability.

As for differing temperaments and persuasions, Deshmukh was no doubt a very different person from T.T.K. as T.T.K. was

from Morarji, and all of them from Mrs Gandhi. I also worked with Sachin Chaudhuri, Y.B. Chavan, H.M. Patel, Charan Singh, Bahuguna, Venkataraman and Pranab Mukherjee—different persons all. And practically all of them gave me my due and some, a great deal of affection over the years. The reason for this happy experience must surely be found largely in one of T.T.K.'s astute remarks: we were all—civil servants, experts and ministers—product of a middle class nurtured by the nationalist struggle.

Apart from personalities and personal equations, were there really sharp differences among these people, in strictly economic matters? Even between Morarji and Mrs Gandhi, there were no great policy differences till 1969 when political exigencies led to the split in the Congress Party. After that, things became confrontational, exaggerated and ideological in overtones. Much of the so-called policy divide, however, was cosmetic and rhetorical and designed to obtain political mileage. Neither Panditji nor Mrs Gandhi were really socialists of the Marxist or Soviet hue. And Morarji, when he became the Prime Minister in 1977, did not dismantle any of the essential features of Panditji's or Mrs Gandhi's policies. Planning was continued. Relations with the Soviet Union (as also with the US, China and Pakistan) were maintained and even improved upon; and the superstructure of nationalization, including that of banks, remained intact.

The story of Indian economic policy from Independence to the present day is one of evolution and continuity—not of revolutionary or sharp turns in direction. It reflects Indian realities. Its size, diversity and democratic aspirations and indeed compulsions, all make for compromise, eclecticism and even incompatible cohabitation. It needs a big smack or an electric shock for a huge and complex animal, say the elephant, to make it change its direction—and then, too, only slowly.

At the London School of Economics, I was pressed by a journalist to declare myself in ideological terms. On the spur of the moment, I said that if I had to describe myself, I would call myself an old-fashioned socialist. I could as well have said that I was an old-fashioned liberal. What I meant was that I was not a Marxist

socialist opposed to markets and private property. But I was not a card-carrying capitalist either, and was supportive of certain values like compassion and justice in all social and economic arrangements. That was and still remains the mainstream intellectual and indeed political opinion in India.

Even in so far as planning was concerned, few were opposed to giving Mahalanobis's ideas a try. There were misgivings. But the underlying ambition for a bold plan for broad-based industrialization was shared by most of us. There were more serious differences of opinion on licensing and controls. But even here, the protagonists began soon to be disillusioned. By 1966 at least, the predominant economic opinion was in favour of decontrol and deregulation. Why this movement did not gather momentum needs a more detailed analysis than I can attempt here. But the reasons lay largely in circumstance rather than conviction.

Certainly, there were moments of sadness like the dismantling of gold control or when T.T.K. or Morarji had to resign. There was also sadness when the promised non-project aid did not follow devaluation or when the Bangladesh crisis set us back a few years. The sadness one felt with progressive debasement and politicization of all institutions and the rising tide of corruption, alas, continues. But not all or even most of these events had their roots in fundamental differences on economic policy.

In the ultimate analysis, it is your own temperament that shapes your behaviour and destiny. I learnt from my father not to be judgemental—that even those who betray or hurt you may have a good reason, that there is always another side to everything. My family teases at me for always enunciating the pros as well as the cons—for seeing both sides of the coin at the same time, so to speak. I learnt from my mother on the other hand that there are things about which one has to feel strongly. But how can you be passionate about anything without being blinkered? On the other hand, how can you avoid being cold and indifferent and inactive while trying to eschew judgements? It is not easy to strike a balance. But one tries as best as one can.

Index